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STUDIES IN WORLD ECONOMICS

BY

G. D. H. COLE

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FOREWORD

THROUGH most of the essays which appear in this volume there runs a common idea—that economic conceptions and the theories built upon them need far-reaching revision in the light of the developing forces in the world of to-day. For most of the familiar economic concepts of to-day are the products of thought upon past situations, belonging to past phases of industrial growth. I have tried, in these studies of a number of economic problems of to-day, to keep constantly in mind the essentially historical basis of economic thinking, and to break away from traditional concepts and methods of treatment wherever they seem to be no longer the right clues to the understanding of contemporary economic facts. With these few words of explanation I am content to let the essays stand by themselves.

Most of them have appeared previously, in whole or in part, in various publications. But I have in all cases worked over the material again, and in many made large changes. Thus, I am indebted to the Editors of the *Encyclopaedia of the Social Sciences* for permission to use again the articles on 'Industrialism', 'Inheritance', '*Laissez-faire*', 'Economic Mobilisation', and 'Socialisation'; but the first two of these have been retouched, and the other three substantially revised. The greater part of 'A Short Study in World Economics' originally appeared in the *New Statesman and Nation*; but I have made changes and added a new section. 'Our Unused Wealth' is also based on a *New Statesman* article; but it has been completely rewritten and expanded. 'The Problem of Consumers' Credit' is partly new, and partly based on a rewriting of several articles from *The Christian Century* and *The Millgate*. 'Loyalties' was originally a paper read to the Aristotelian Society, and published in its *Proceedings*. 'Economics in the Modern World' (from

the *Political Quarterly*), 'The End of the *Bourgeoisie*' (from *The Student World*), 'The Planning of International Trade' (from the American *Foreign Affairs*), and 'The Economics of Advertising' (from a source which I regret to have forgotten, and therefore to be unable to acknowledge) appear substantially in the forms in which they were first published. 'Dr. Hayek's Triangle' and 'Towards a New Economic Theory' are entirely new.

I desire to thank those who have given me permission to use the materials published elsewhere which I have incorporated in these essays. Selected from a much larger body of occasional writing, they form, I hope, enough of a coherent presentation of a point of view to be worth offering in book form. In a sense, they continue and amplify the criticism of contemporary doctrines and institutions in my earlier *Economic Tracts for the Times*.

G. D. H. COLE

OXFORD, *February* 1934

CONTENTS

I

A SHORT STUDY IN WORLD ECONOMICS[1]

I

Capitalism on its Trial

All over the world to-day the capitalist system is on its trial. It is in peril of its life not only in Europe, where it has long had to meet the challenge of an active Socialist movement, but also in the United States, where until almost now its position has appeared impregnable. For Socialism has never yet become in America a force to be reckoned with; and until only the other day Socialism, based on the working-class movement, seemed to present the only serious challenge which Capitalism had to meet. But now the situation has become far more complicated than the simple confrontation of Socialism and Capitalism made it out to be. For not only has Socialism itself divided at the crossroads of the Russian Revolution into two separate and often antagonistic movements, but also there have arisen, and are arising, new forms of Society which it is a puzzle to categorise aright. Is 'National Socialism'—which, whatever it may be, is certainly not Socialism—a form of Capitalism, or a new third alternative to the previous antagonists? And is the new order which President Roosevelt is trying to set up in the United States, as a way out of the present depression, merely a re-shuffling of the capitalist pack, or the beginning of a new system which will differ so from the old capitalistic Society as to merit a new name?

It is extraordinarily hard to give a confident answer to these questions in a situation as confusing as that of to-day.

[1] Based on a series of articles originally published in the *New Statesman and Nation* in 1933.

Or rather, it is simple enough to give an answer, if one is content merely to apply old categories to new situations, without going to the trouble of thinking things out afresh; but it is very hard to think clearly about new forces which are only now beginning to define themselves in action. For at any rate in politics no force can be really defined till it has been tested by practical experience. What can be seen is that the present world situation quite lacks the simplicity attributed by the traditional analyses, and is therefore discomfiting both to the advocates of capitalist *laissez-faire*—above all to the theoretical economists and the orthodox financiers of the old order—and to Socialists who have grown up unquestioningly in the rival orthodoxy of Marxism. For, whereas the former have to reckon with the patent fact that the capitalist system, under present conditions, does not work, or works at any rate so badly as to be in constant danger of ceasing to work at all, the Socialists are in the quandary of finding that the growing difficulties of Capitalism do not necessarily bring with them, at least in the short run, the triumph of Socialism, and that the simple conception of Society as divided between capitalists and proletariat—the Haves and the Have-Nots—by no means adequately expresses the actual divisions of economic classes in the advanced industrial Societies of to-day.

Orthodox Social Democrats are, indeed, in a more confusing theoretical pickle than the stalwarts of private enterprise. For while professors and bankers continue to tell the world, in a mournful chorus, that all its troubles arise from not letting ill alone, and so suffering it to be transmuted mysteriously into good, the Social Democrats hardly know whether they are standing on their head or their heels. First, there was the awkwardness of the Socialist Revolution happening first of all in the wrong country—in a country which, according to the recognised rules, was demonstrably 'unripe' for Socialism. Then there was the growing tendency of many people in many countries to question the basic assumptions of the established theories

of parliamentary democracy which the Social Democrats had taken over from their Radical predecessors. Thirdly, there was the eclipse of Socialism and of the organised working-class movements on which it relied for its driving force, first in Italy and then—far more disastrously—in Germany as well. And fourthly, there was, in the countries which did not fall a prey to Fascism, a growing sense of stalemate; for the Socialists, having advanced far enough to prevent the capitalist parties from governing in a purely capitalist fashion, had to realise the great difficulties which still remained in the path of their further advance to a definitive conquest of political and economic power. Socialists found themselves forced to assume, far sooner than they had expected, the responsibility of governing—on condition of doing so according to capitalist principles, and refraining from any real attempt to set up a Socialist system. Or they had to support capitalist Governments of the 'Left', in order to avoid the return to power of Governments of the 'Right' more hostile to working-class claims. They had, in fact, to try to make the capitalist system work better, though their supposed *raison d'être* was to destroy it, because they did not feel, and were not, strong enough to replace it by an alternative system of their own.

Yet these accumulating troubles of the world's Socialist movements do not at all serve to free the capitalist system from its anxieties. For the strongest card of the defenders of Capitalism has always been that, despite all its imperfections and injustices—which are not denied—it does somehow on the whole contrive to 'deliver the goods'. That, however, is just what to-day it is obviously failing to do. For, in face of an unprecedentedly rapid advance in productive power in both industry and agriculture, which ought in plain common sense to yield to every section of every community a rapidly rising standard of life, the wheels of production have slowed down, unemployment and distress exist on a scale unknown to living memory, and every nation is engaged, not in making the most of the new opportunities for wealth, but in an undignified, and

for the most part unsuccessful, scramble for shelter from the universal storm.

In these circumstances no thinking man can rest satisfied with Capitalism as it is, or respect a system which, having the means to produce abundance, can find no way of distributing the wealth that is its for the taking. The intellectual case against Capitalism thus becomes overwhelmingly strong, and is reinforced every day by the spectacle of economic and political futility which the capitalist world presents. It does not take a clever man to see that there must be something radically wrong with a system which holds it 'cheaper' to maintain many millions of people in idleness than to set them to useful work, and wrings its hands, not because goods are scarce, but because it can find no means of agreeing, by concerted restriction of output, to remove the curse of plenty which has fallen upon it.

Intellectually, and by way of practical object lesson, the traditional capitalist defences are down, and the orthodox defenders of the system as it is are growingly conscious of the certainty of defeat, unless they can find reinforcements. But, though the wall is breached, are the Socialists strong enough to take the citadel? The German Socialist movement was reputed among the strongest in the world; and German Capitalism was undeniably battered and broken. But Hitler, and not Otto Wels, led his storm troops to the conquest of the Weimar Republic, even as Mussolini, ten years earlier, had easily routed the divided and hesitant forces of Italian Socialism. Moreover, whatever system is destined to emerge out of the courageous opportunism of President Roosevelt's policy in the United States, it will certainly not be Socialism in any sense hitherto attached to the word. State-controlled Capitalism, perhaps; or perhaps something so different from anything the world has known or thought hitherto as to require a new name. But Socialism, built on the class-struggle and using as its instrument the working-class movement—that, assuredly not.

It is too much, no doubt, to hope to distil clarity out of the muddied waters of the world of to-day; but we can, and

must, at any rate make some attempt to evaluate the forces that are at work. It is useful to put the right questions, even if we cannot at present find complete or satisfactory answers; for, as any thinker knows, putting the right questions is the first essential step towards clearing up a problem, and wrong questions, far more than wrong answers, are at the root of false and unproductive thinking. What, then, are the vital questions which we must ask ourselves, if we are to set out on the right road towards a solution of our difficulties?

First and foremost, out of all the many things that are amiss with the world to-day, which is fundamental? Which, that is, underlies and is chiefly responsible for the rest? Secondly, what forces are at hand, and can be used to best advantage, for putting right the fundamental evil, whatever we may discover it to be? Thirdly, what forces stand chiefly in the way of putting it right, and can these forces be amended and turned into instruments of the sound policy, or must they be simply fought and overthrown? And, finally, what is, within the limits set by inescapable facts of human and physical nature, the kind of new Society we want to build? Many, I know, would put the fourth question first. I put it last, because I am certain that it is merely Utopian to devise a new pattern for Society, save in the light of the present evils from which men are seeking to escape, and of the forces with whose aid, or against whose opposition, any advance will have to be made. That is, in effect, to say that theories and ideals, if they are to be fruitful, must arise out of solid facts and living forces, and be re-made by each generation in terms of its own problems and of the materials that lie ready to its hand.

II

The Limits of Monetary Reform

We come, then, to our first question. Of all the many things that are amiss, which is fundamental, and comes

nearest to explaining and including the others? We are not, of course, expecting to find a single, all-embracing cause; but it is not hard, I think, to find a provisional answer that goes deep enough for our purpose. It is, quite simply, that Capitalism, as it is organised to-day, is not making men rich, but keeping them artificially and absurdly poor. It is lamentably failing to use the great opportunities for the creation of wealth which the advance of science has placed at its disposal; and, even when it does seek to use them, it often turns them into curses by making them the means to futile destruction in war or, in peace, of displacing and disemploying workers, for whom it provides no alternative sphere of useful service. Making the profit of a limited body of owners, and not the production and distribution of the largest amount of wealth and welfare, its direct object, it inevitably seeks scarcity and not abundance; for it is scarcity that makes things dear and profitable to their owners. But when it fails, despite all its efforts, to make things scarcer than the means of buying them, the only remedy it can think of is enforced restriction of output, in order to restore the lost blessing of dearness. It chases endlessly after its own tail in an endeavour to abolish goods faster than it abolishes the incomes of the consumers; for it is unable to grasp the fundamental truth that things cannot on the whole cost more than people are able and prepared to spend on them.

We have, then, as our root evil the sheer failure of the capitalist world to deliver the goods to the general body of consumers. But at once the question arises whether this failure is due to a fault in the monetary mechanism of Society, or to a radical wrongness inherent in the capitalist system as a whole. It is obviously tempting, especially for those who find themselves reasonably comfortable under the existing conditions, to attribute the evil to monetary causes, which look as if they could be removed without a sharp break with the existing economic order and its complete supersession by a different system. For, even apart from motives of self-interest and fear of the unknown,

most people have in them strong conservative instincts; and in addition money, being by tradition something of a mystery, lends itself readily to mystifications and to plausible jugglings with formulae guaranteed to set the world to rights.

There are, however, strong reasons for holding that, while there is much amiss with the existing monetary system, the evils of the present order go far too deep to be cured by any alternative method of monetary management. For, in the first place, despite the assertions of some of the monetary reformers, there is under Capitalism no persistent shortage of purchasing power in relation either to the volume of goods on the market or to the productive ability of Society. There is, on the other hand, a tendency to alternation between an excess and a deficiency of purchasing power, corresponding to the alternate expansions and contractions of bank credit. In booms credit is expanded so far as to raise prices without a balancing expansion of output, while in slumps its effective use is so curtailed as to cut off demand and cause production and employment to be seriously reduced. That this is a grave fault in the present mechanism of the monetary system is clear enough; but whence does it arise? It is due at bottom not to a purely monetary cause, but to the inherent instability of the capitalist order. Bankers cannot effectively create money unless there is a demand for it; and the business demand, under Capitalism, can arise only from the expectation of being able to use it at a profit. For the most part the bankers, in creating more or less money, are following, and not initiating, the rise and fall of profit-seeking demand from the capitalist *entrepreneurs*.

It is, of course, true that, for some time past, a deliberate attempt has been made to bring back prosperity in the United States by means of monetary reflation, and that bankers can do something, by the mere emission of additional credits, to give an impetus to business optimism and trade revival. But the events in America during the past few years sufficiently show that, if a forward move-

ment generated by these methods is not speedily to collapse, other forces besides the emission of more money must be brought into play. Already it is realised in the United States that, unless steps are taken at once so to raise wages as to bring about an effective expansion in consumers' demand for the products of industry, and also by extensive public works to create demand for the services of the constructional trades, reflation is bound to end in ignominious collapse.

But, some people will argue, this only shows the more that our present monetary system is on the wrong lines. For the system pumps out credit only to producers, whereas what is needed is a supply of 'consumers' credit'. At this point we must beware of confusion—of using the word 'credit' in two different senses. For the essence of producers' credits is that they are repayable loans; whereas what the advocates of consumers' credits want is that there should be additions to purchasing power carrying no obligation of repayment at a later date. Otherwise, why go beyond instalment purchase, which has been in fact used on a large scale as a method of issuing repayable consumers' credits—much to the subsequent sorrow of those who were caught in its meshes?

The issue of non-repayable credits to consumers would necessarily upset the existing relationship between costs and incomes; for it would create a supply of purchasing power that would in no way enter into costs. If there were in fact a permanent deficiency of purchasing power under the existing system, this would be all to the good. But there is not: there is an alternation of deficiency and excess. If fresh purchasing power not entering into cost were created in the consumers' interest, it would express itself in an additional demand for goods. But the production of these goods would involve additional costs, which would also swell purchasing power. Accordingly, the prices of goods would rise. If the policy were begun in a period of depression, this too might be an advantage; for as the increase in purchasing power would be greater than the

increase in goods it would provide an additional profit stimulus to the employer to expand production and take on more men. But this could only go on until all the available productive resources had been brought into use, and on condition of allowing prices to rise enough to bring them into use. When this had happened, the issue of consumers' credits would have to cease altogether; for to continue it would inevitably inflate prices without further increasing production.

This may appear to give the advocates of consumers' credit their case, as far as the present depression is concerned. For it does admit that this method could be used to raise consumers' demand, and to bring additional production into being. Indeed, I am sure this is the case: only I would rather use the new money, with more considerable effect, for the carrying out of useful public works, which would not only mean paying out wages and salaries but also stimulate the required revival in the constructional trades. A great national housing scheme, for example, would satisfy all the conditions of soundness in the present situation.

But while I agree that a capitalist revival could be stimulated by these methods, I believe it would have in it the inescapable capitalist tendency to generate a renewed depression. For the root fault of Capitalism is that it leads, as soon as it becomes prosperous, to a self-destructive maldistribution of income. The difficulty is not that there is not enough purchasing power to buy the available supply of goods, but that this purchasing power is wrongly distributed—too much to the rich, and too little to the general body of wage-workers. This mal-distribution results in an attempt by the capitalist recipients of income to save and invest in times of prosperity an unduly large part of the total available purchasing power. But investment is of use only if consuming power expands fast enough to buy the increased supply of goods which is produced with the aid of the enlarged capital equipment. If a large part of the new purchasing power that is created during a boom is

invested, this means that it buys in the first instance capital goods and not consumers' goods, though of course it soon works round, by way of additional wages, to create an increased demand for consumers' goods as well. As long as the upward movement continues, the desire to buy capital goods increases faster than the ability to buy the consumers' goods which they are to be used to make. As soon as this lagging behind of consuming power comes to be realised, a slump ensues; for the expectation of profit from the making of more consumers' goods disappears, and in the long run the demand for capital goods therefore falls off as well—for it depends on the demand for consumers' goods. Capitalists, instead of investing their savings, leave them idle. Many capital values are written off or down by bankruptcies and business losses; and again there is widespread unemployment and disuse of productive resources.

This endless cycle of capitalist boom and depression is often exaggerated by bad banking policy; but what lies at the root of the trouble is not the mismanagement of the monetary factors, serious as it is, but the inability of Capitalism to provide at one and the same time a sufficient profit incentive to get all the productive resources employed and a distribution of purchasing power which will enable consumers' demand to expand in due proportion to the advancing productivity of the economic system. For this reason, while it may be possible, by largely monetary means, to turn a slump into a boom, it is not possible to do this without bringing again into play the inherent capitalist tendencies which will lead on to a new slump. Or, if we cannot yet take that point as proved, let us say only that a boom which will not generate a new depression is impossible for Capitalism in the forms in which it has existed hitherto. Whether it is possible for a revised and amended Capitalism we must go on to consider next.

III

State Capitalism and Capitalist Planning

Nineteenth-century Capitalism was proud of being without a plan; for it held that all the required planning was done for it by an 'invisible hand', with whose dispositions it would be blasphemy as well as folly to interfere. But to-day economic faith in Providence is at a discount, with little prospect of a return to the 'gold standard' of the old trust in the virtues of the competitive principle. Accordingly, for some years past we have been hearing of a strange new economic type—the capitalist advocate of a planned economic system. These capitalist planners have been influenced in part by the great growth of trusts and combines, which claim to have established an ordered system of production over large tracts of industry, and partly by the example of the Socialist Five-Year Plans in Russia. For, say the capitalist planners, if Socialism has a plan, why should not Capitalism have one too—and so both reap all the advantages of planning and stave off for ever the danger of a Socialist victory?

The first thing to observe about capitalist planning is that it involves a complete throwing over of all that part of the capitalist philosophy which the defenders of the system have hitherto put in the forefront of their argument. For whereas every Socialist, pink or red, is by absolute necessity a planner, capitalist planning is a highly paradoxical idea. If private enterprise and competition are to be eliminated over the greater part of industry, as all Socialists urge, planning follows as a matter of course, as the only possible alternative method of economic regulation. If production is to be a public concern, the public must, through appropriate organs, decide how much of each kind of goods to produce, what prices to put upon them, what pay to accord to their producers, how much to set aside for capital accumulation, and how much to

devote to immediate consumption. It must, in fact, regulate by means of a comprehensive plan all the vital matters which have in the past been settled by individual or group action and individual or group competition under 'private enterprise'. The capitalist planners now agree that these things, or most of them, must be regulated in accordance with a comprehensive plan; but they do not see why this should not be so done as to leave the ownership and management of most industries in private hands, and without any radical change in the distribution of incomes, such as Socialism always connotes.

But will Capitalism, which has in fact drawn its strength from leaving room for the free play of private economic forces, continue to work at all when it is confined within the limiting conditions of an enforced general plan? As long as industries are carried on by private enterprise, with private profit as the incentive to production, can the State, or any other authority, successfully issue orders to the capitalist about what he is to produce, or refrain from producing? Of course it can, up to a point; but can it without destroying the incentives and deterrents which alone have kept the capitalist system up to the scratch? What is to happen if the Plan decrees that the capitalist shall produce something the making of which will involve him in a loss? The State can doubtless, up to a point, deal with this difficulty by guaranteeing the capitalist's profits; but will not any such guarantee fatally destroy the incentive to efficient production, and so bring about a hopeless ossification of the capitalist system? What will happen is either this ossification, or a rapid transformation of the employer into a mere manager on behalf of the State—in other words, a development of Planned Capitalism into State Capitalism.

It does not, however, follow that State Capitalism is an impossible system. Its outstanding differences from Socialism are two, one superficial and one profound. The superficial difference is that it will probably go on using capitalist terminology of the old kind, dubbing men employers

when they are really only managers, and calling joint stock companies what are really State concerns. The fundamental difference is that it will seek to preserve the existing class-divisions and inequalities of income, though these will have become grossly inappropriate to the conditions of the new economic system—for the capitalist shareholders and directors will have become simply functionless and superfluous when they are no longer even nominally responsible for directing the course of production and investment.

Can any system which involves this evident incongruity last? It will continue to be exposed to the same danger of generating slump out of boom as afflicts capitalist industry to-day, save to the extent to which it can reconcile itself to altering the distribution of income drastically in favour of the wage-earning class. If it fails to do this, it will go down to defeat at the hands of the depressed. But even if it does accomplish the miracle of making capitalists believe in high wages, will it not go down to defeat all the same? For will not the workers use the power which comes of high wages and full employment to bid the functionless classes above them get off their backs, and to insist on taking over the control of the economic system themselves?

There is one condition on which this might not happen—that the directing groups at the head of the planned State-capitalist system should be successful in hiding the incongruity of their economic arrangements by calling other elements in men's nature into play. If men can be made to feel more aggressively Nationalist than class-conscious, they may be induced, in the name of the 'National Idea' and the 'Totalitarian State', to refrain from challenging the injustice of the economic order. This is the calculation on which Fascists and Nazis alike base their economic programmes. But I believe the Nationalist spirit can be raised to this pitch only if it can be made to feel itself constantly beset by a host of enemies—whether they be other nations around, or Jews and Marxists, suspect of

internationalism, within the gates. As long as men are afraid, excited, kept up to a pitch of nationalistic fervour by rumours of war, pogroms, and ceaseless 'Hymns of Hate', the trick may be successful; and its prolonged success by these means may avail to break civilisation in pieces. But there is in this sort of Nationalism no real permanence: it must either explode in destructive warfare, or begin before long to simmer down. And, when it does begin to cool, the economic factors will speedily reassert themselves, and the countries that have tried to keep them back will be faced again with the old dilemma; for they will have to choose between the wrecking of their incongruous system by economic failure, and its destruction by economic success.

There is, however, one qualification which must be introduced at this stage. A deficiency of widely diffused consuming power need not mean a slump in a country which is in a position to export a large proportion of its low-wage products without receiving equivalent imports; for it can then make up for its own lack of consuming power by some other country's greater abundance (provided, of course, that its capitalists are prepared to export enough capital to balance its excess of exports). But such a situation is essentially precarious; for it implies that other countries are prepared to accept an excess of imports, and have enough consuming power to do this without throwing a substantial number of their own producers out of work. That this is an unlikely supposition the prevalence of high tariffs in the countries with high wage-standards clearly shows; for these countries cannot keep up their own wages if they allow unrestricted competition of low-wage imports. Accordingly the pursuit of the policy of export-dumping in order to offset a deficiency of domestic consuming power is bound to be self-destructive, if any substantial number of countries resort to it. It can lead only to the general victory of an extreme Economic Nationalism which is incompatible with its lasting success.

That Economic Nationalism is incompatible with this

policy is a point of importance; for it means that countries which follow a policy of Economic Nationalism must become, within the limits of their productive power, high-wage countries if they are to survive, because they will have to depend on the consuming power of their own home markets. Their ability to afford a high standard of living may be reduced by Economic Nationalism, which involves forgoing the advantages of the international division of labour. But out of their diminished resources, they will have to pay out a larger *proportion* in wages and other forms of widely diffused consuming power than they would if they were working within an international system of the nineteenth century type. That is, fundamentally, why I hold that some sort of Socialist tendency is bound, in the long run, to assert itself within the Fascist or Nazi States, however thoroughly the rulers of such States may set themselves to extirpate the existing Socialist and Communist movements.

The case of the United States calls for separate consideration; for it seems to be approaching Economic Nationalism by a quite different road, with an attempt at the outset not to crush the working-class movement, but rather to insist on a rise in wage-rates in order to secure as soon as possible an expansion of consuming power up to the limits of current productive capacity. If this can indeed be done, and the position held thereafter in moving equilibrium—for wages must go on advancing as productivity improves, and must be raised further to balance any tendency to decrease the total wages-bill through greater mechanisation of industry—then indeed the prospect of a stably revived system of State-controlled Capitalism is opened up. For it is doubtful if, under such conditions, the American working class would, at any rate for some time, even wish to supersede the capitalist system.

But is this vision at all likely to be realised? I doubt it. American business can be induced to accept drastic Government control, and to raise wages, as long as it is in a bad way and is hoping for salvation at President Roosevelt's

hands. For it realises that it cannot have one part of his policy without the others. But let President Roosevelt succeed in 'reflating' the United States back to prosperity, and then we shall see! Will not the American business man, once the panic is over and his 'confidence' restored, promptly throw over the controls to which he has submitted in the emergency, and joyously revert to the type of Capitalism which landed him in such a pickle in 1929? My feeling is that he will, and that American individualism still goes too deep to be eradicated at a single sweep of President Roosevelt's operating tool.

I hold, then, that, while Capitalism can on certain conditions reflate itself back to a temporary and unstable prosperity, and while State capitalist systems based on extreme Economic Nationalism may be successful in establishing themselves for a time, all these systems are bound to be precarious and evanescent, and to bring the world back to the fundamental problem of devising methods of economic government which will give it a more assured and better diffused prosperity. Is Socialism such a system? That is the question I shall ask, and try to answer, in the concluding sections of this essay. And I shall ask, too, what are the prospects of the world actually turning to Socialism as a remedy for its disease.

IV

The Case for Socialism

Has Socialism in it, what Capitalism finally lacks, the means to the establishment of a stable prosperity? I think it has, because Socialism, unlike even the most highly controlled Capitalism, is based on bringing *all* the vital factors under collective control, and relating its entire economic policy to a single, simple, and satisfactory objective. The fatal weakness of controlled Capitalism is that, moving still within the orbit of the profit system, it is compelled to subordinate its use of the available factors of production to

the exigencies of private profit-making. This causes it to look with very different eyes on the two 'key' kinds of income—profits and wages. For, whereas profits appear to it as an undiluted good—*the* stimulus *par excellence* which causes production to be undertaken—as well as a necessary element in the available supply of purchasing power, wages on the other hand appear to it evil as well as good. They are good, in that they are a form of purchasing power, necessary to create a demand for the products of industry; but they are also bad, in that they are a cost which the business man has to incur, and therefore a deterrent to production. For it inevitably seems to the business man that the higher the wages, the less is the prospect of profit, and the smaller the incentive to expand production to the furthest point compatible with the supply of productive resources.

This dualism, I am sure, is the fatal flaw in modern Capitalism. But it is a flaw from which a Socialist economic system will be able to make itself entirely free. There will, of course, still be costs of production under a Socialist system, and it will be no more possible for socialised industry as a whole than for any other kind of industry to sell its products for less than they cost to produce. But under Socialism all incomes will be costs, and all costs incomes. There will be no such distinction as exists to-day between incomes derived from profits which are a *surplus* over costs, and other forms of income which need to be kept as low as possible because they are costs which eat into this surplus. It will be apparent to everyone that there is a certain amount of real income available for distribution, that this is simply the money name of the total supply of goods that is actually produced, and that it is accordingly to the general interest to make this supply of goods as large as it can possibly be made. A situation in which it 'does not pay' to use available resources of production simply will not be able to arise.

Such a situation can arise under Capitalism only because the capitalist view of what 'pays' depends simply on the

amount of profit, *i.e.* of surplus over costs, to which an act of production gives rise. Suppose a capitalist produces something, incurs £x in costs of production (wages, interest, rent), and sells the product for £x, then, according to the capitalist reckoning, production has not been worth while; for there is no surplus. But from the collective point of view it has been well worth while; for by the use of certain available resources, which would otherwise have been left unused, £x of real value has been created and £x of purchasing power distributed to buy it. Of course, it would not 'pay' from any point of view to incur £x of costs in order to produce £x of goods if the same expenditure of productive resources could be used to create goods worth £$x+1$; but it would pay better to use the resources at a cost of £x in order to produce £$x-1$ of value if otherwise the unused resources would cost more than £1 to maintain in idleness.

This simple piece of economic reasoning is one to which only a Socialist system can give practical effect; and precisely for that reason only a Socialist system can solve the problem of using to the full the great and rapidly advancing productive resources which are at the disposal of mankind. For only under Socialism can the problem be seen clearly as one of distributing the available productive resources so as to yield the maximum amount of useful goods, and of distributing incomes on the scale required to create a demand for all the available supply of goods and services—neither more nor less.

The principle is simple; but, of course, the problem of giving effect to it is highly complex. For a Socialist system will have to manage and harmonise the three vital parts of the economic process—the production of goods and services, the distribution of incomes, and the pricing of goods and services so as to make demand and supply balance. Clearly these three things must be co-ordinated aright if a Socialist Economic Plan is to work. And no less clearly the right solution of each depends upon the other two.

In the first place, the Socialist Plan involves the right use of a certain available supply of productive resources.

Now this supply is in part specialised, and can be used only for the production of certain definite things, and in part transferable, so as to be capable of being used, broadly speaking, for any kind of production that seems to be needed. This transferable part is in practice large enough under normal conditions to allow, without serious economic loss, for adjustments in the relative production of different types of goods on a scale sufficient to meet changing conditions of demand. The Socialist problem of production is therefore to plan these changes aright, so as to secure the largest possible production of useful things, in the correct proportions to current demand.

But the nature of current demand for different goods and services clearly depends on what relative prices are set on the various things, and also on how incomes are distributed. In fact, the logically first task of a Socialist Planning Authority will be to plan the distribution of incomes in the community, because, until that is planned, it cannot settle in what proportions the various classes of goods ought to be produced. What has to be planned at this stage is not, strictly, the amount of *money* to be distributed, but the *proportions* in which whatever money is distributed will go to different types of income-receivers—for the actual amounts of money become important only when prices are being fixed.

This is the next stage. The 'general level of prices' must, of course, correspond to the general level of money incomes; and, as long as they do correspond, it does not matter whether they are high or low (under Socialism, that is—for under Capitalism, because of interest and rent, it does matter a great deal). The Socialist problem is the *relative* pricing, within a given general level, of the various goods and services; for on this will, of course, depend the demand for each which a given distribution of incomes will involve.

It will be open for the Planning Authority to adopt any relative prices it thinks best, provided only that total prices correspond to total incomes, and that the prices are

such as buyers are prepared to pay for the supplies of the various goods which the Planning Authority decides to have produced. Within these limiting conditions there will be no *necessity* for the price charged for any particular thing to bear any relation to the cost of producing it. Nevertheless, in the absence of special reasons causing the community to desire to encourage or discourage certain kinds of consumption, costs of production would probably be taken as the main guide in fixing prices; and in any case a strict account would be kept of any deviations from this practice.

The allocation of the available productive resources to various forms of production would thus be settled in relation to the distribution of incomes and to the pricing of the various goods and services. If this were done aright, and adjusted to meet changes in the powers of production and in consumers' tastes and needs, all the essentials of a stable economy, able fully to use its entire productive power, would have been secured.

The criticism will, no doubt, be made that this balancing of the three vital factors is too difficult a task for any Socialist Planning Authority to carry through with success. That there would be mistakes, especially in the early stages, is, of course, obvious. But mistakes would be far less disastrous under such a system than they are under Capitalism. For, if the Planning Authority made a mistake, its immediate reaction would be to correct it by amending its plan of production or distribution or pricing, *and in no case to throw productive resources out of use.* If it 'over-produced' a particular type of goods, it might have to sell off the surplus at a loss, and to shift productive resources to something else as quickly as it could; but it would never be in the position of having to disemploy transferable productive resources on account of a deficiency of demand.

This inherent superiority of Socialism over controlled Capitalism arises above all from its power so to distribute incomes as to create a demand for all the goods that can

be produced, no matter how greatly total productive power may increase. For it is under no impulsion to keep down wages in order to create a profit surplus, or to cause by way of a profit surplus an excess of either saving or investment. It will save precisely what it requires and thinks fit to invest—neither more nor less: there will be no question of investment exceeding savings, or savings exceeding investment; for assuredly investment will be a collective function, and the distribution of the available productive resources will include the allocation deemed appropriate for the production of capital goods before consumers' incomes are distributed at all.

Will the world be induced to resort to Socialism because of its inherent superiority to Capitalism in these respects? Not wholly; for though the failure of Capitalism to solve the problem of distribution, or to ensure stable economic progress, will help greatly in its undoing, the demand for social justice will count as well. Socialism will come, if it comes, not only because Capitalism will plunge into one crisis too many, but also because people will demand with increasing insistence that their real incomes shall rise in correspondence with the rapid advance of real productive power—and because Capitalism, with its necessity to regard wages as an evil, will not be able to respond.

But will Socialism come at all? I do not regard its coming as inevitable. Socialism is, I am sure, the only alternative for our age to sheer economic disaster and the dissolution of European civilisation as we have known it. But it is unhappily possible that we shall allow disaster, even on this scale, sooner than be at the pain of establishing a Socialist system. I think Socialism will come, because it is the common-sense answer to the economic problem. But, in face of the follies of the past two decades, I cannot feel sure.

V

The Outlook for Socialism

The Socialist movement of to-day is divided into three parts—'Old-stagers', 'Communists', and 'The Rest'. The 'Communists' are those who hold that, however remote the prospect of world revolution or of a Communist victory in the Western countries may be, it is the duty of Socialists to preach the inevitability of violence, and to wage truceless war not only on the capitalist system but even more on all Socialists who will not completely accept their dogmas and their strategy. The 'Old-stagers', on the other hand, are those who, having grown up inside the parliamentary parties of Social Democracy and Labour, and pursued all their lives a policy based on the assumption that their cause would advance gradually to the conquest of a parliamentary majority, have lost the power of thinking in other than parliamentary terms, and remain impervious to every sign and portent of the contemporary political chaos. 'The Rest', in whom the hope for Socialism lies, are at present a motley crew, lacking unity or clear definition of purpose, but prepared at any rate to think freshly, as need arises, in terms of a constantly changing political and economic situation. Their strength lies in this—that they, far more than either of the other groups, are receiving constant reinforcement from the young and from the new recruits whom the manifest failure of Capitalism brings over to the Socialist side.

'The Rest', at present, lack a coherent policy; but on their getting one the hope for Socialism depends. For the old politicians of the Labour and Socialist Parties are manifestly played out; and the Communist strategy is obviously inappropriate to the class-structure of the countries of Western Europe. Socialism will come in Western Europe, if it does come, as a product not of increasing misery among the unemployed, but of increasing resent-

ment at the sheer idiocy of the capitalist system. For Socialism cannot conquer a majority merely by appealing to the 'down-and-outs'. In advanced countries, it can win only if it can gain the support of the main body of relatively well-off workers and also a substantial fraction of the professionals, technicians, and other 'blackcoats' who constitute a large and growing element in the more developed economic Societies.

Indeed, the rise of Communism among the 'down-and-outs' is far more likely, in the short run, to lead to Fascism than to Socialism. For it will raise up against it the fears of the entire middle class, and enable them to sidetrack Socialism by an appeal to crude nationalist instincts. In economically advanced countries, it is fatal strategy for Socialists to rally, against the manual-working class, the entire forces of the upper and middle classes, the farmers, the small *rentiers,* the wage-earners whose occupations depend on the maintenance of the *bourgeois* standard of living, and all the discontented who see in Fascism a better chance of personal advancement and self-expression than the Socialist movement seems ready to provide. In Great Britain or France or Holland, to win recruits for the Communist Party is not to forward the cause of Socialism, but definitely to set it back.

But it is no less true that the dronings of the Socialist 'Old-stagers' have in them no suggestion of an impending victory. Less and less do they stir political enthusiasms, or inspire confidence in the real will of the Socialist Parties to make the world new. For these 'Old-stagers', looking at the situation from the standpoint of an electioneering experience gained under very different conditions, and highly diffident of their own powers, are far more intent to avoid promising more than they feel equal to performing than to present an effective challenge to the capitalist order. They want to look as undangerous as possible; but to look undangerous is, in the result, to look ineffective. For assuredly the world needs not merely changing, but changing rapidly and with courage.

Rapid change does not at all, either in Western Europe or in the United States, involve the discarding of parliamentary methods or of political democracy based on parliamentary institutions. But it does involve using these methods and institutions in a radically new way; and it is of vital importance to distinguish between the supersession and the adaptation of the parliamentary machine. The opponents of Socialism are, of course, eager to obscure the difference, and to represent the advocates of a new use of Parliament as would-be dictators, who have declared war on democracy. To introduce this confusion is the obvious strategy of the reaction; for faith in parliamentary methods is still strong enough in the West to render those who challenge them suspect of all manner of strange designs. But there is in reality no need to challenge them; for Parliament is undoubtedly under present conditions the appropriate instrument for an advance towards Socialism. What is needed is the working out of a new parliamentary strategy, based on the recognition that the change to Socialism needs to be made far more rapidly and decisively than seemed needful, or even possible, before Capitalism had entered on its present phase of decay.

This new strategy has to be so conceived as to enable things to be done both quickly and in decent order. It has to offer the small property-owner the assurance that he will not be treated like the *kulaks* in Russia, but will have his position carefully safeguarded during the transition to a Socialist economy. It has to offer the technician the assurance that the socialisation of the major industries will give him the chance of doing his job better than before, because he will be less trammelled by the short-sighted avidity of the shareholder or the manipulations of the financier to whose mind production is no more than an incident in the money-making process, and that he will be far more free to let the rapidly advancing productivity of industry issue in an increased output of useful goods. It has to offer to the wage-earner the assurance of a better

distribution of wealth, and the prospect of regular useful employment at a rising standard of life in ministering to real human needs. It has to offer to every person who abhors waste, untidiness, and profitless diffusion of effort the promise of an ordered economy directed to making the best use of all the available resources of production.

All this implies a Socialism forthright, and yet careful and expert, promising enough, but not too much, relying for its ability to deliver the goods on the great unused productive powers that lie ready to be called into play. This Socialism must be prepared, above all, to think realistically about class-divisions in terms appropriate to its own place and generation. It must realise that, if the 'proletariat' means merely the 'down-and-outs', then it is impotent to establish Socialism by itself; that if the class-struggle implies the simple confrontation of two classes, the 'Haves' and the 'Have-Nots', in a Society from which all intermediate groups have been eliminated, then it is based on a gross distortion of the facts; and that, if the working class means only the industrial manual workers, they may whistle for Socialism unless they can find allies.

For the idea that Socialism will drop, in due time, like a ripe pear from the tree is, or should be, utterly discredited. It remains true that Socialism—that is to say, a planned economy based on public ownership and control and the nearest practicable approach to equality in distribution—is the appropriate answer to the world's present economic difficulties, because it alone promises not only a way of ending the depression, but also the establishment of a stable and balanced economic order as a safeguard against future slumps, certain to lead, sooner or later, to complete and irremediable collapse. But the mere fact that Socialism is the appropriate answer does not show that it is the answer which mankind will make. For there are, in the short run, other possible answers, which may be effective in making the capitalist system work again for a time—and it is always possible that, if Capitalism fails

to work or generates a new world war, Western civilisation will tear itself to pieces fighting in order to save itself the trouble of thinking its problems through to an end. Socialism, whatever it is, is assuredly not inevitable. It will come, if it comes at all, only as the reward of hard work and thought and conscious striving among a sufficient number of bold and intelligent people.

Moreover, if the world goes on as it is going to-day, with a rapidly increasing emphasis on Economic Nationalism, the Socialist movements in the various countries, however fully they may keep their internationalist ideals, will be driven to accommodate their practice and policy to the differing national conditions they will have to meet. Socialism, even against its will, will become more divided by national frontiers as Capitalism itself becomes more divided. For each country will have, with only secondary help from others, to work out its own national salvation; and internationalism will be rebuilt, if at all, only as a result of national victories for a cause compatible with it. Socialism aims at an international system, or even a cosmopolitan. But it will have to go round about, because the world in which it is struggling has divided its forces into separate national groups, and within each of these Socialists must in the main win their way to power.

There is, of course, in this situation a danger of a purely 'National Socialism', such as the Nazis used to acclaim, but show few signs of practising. But this danger is remote, except in the form of a State Capitalism which may borrow some Socialist measures, but will turn them to uses compatible with the retention of class-divisions and of a capitalist social structure. The Socialism for which the Socialist movement stands remains international, however much it may be compelled to work on national lines. It remains, for example, strongly pacifist in a world given over again to increasing armaments and renewed threats of war. If Socialism wins, internationalism wins too, however greatly the new internationalism based on positive collaboration between planned and organised Socialist States

is certain to differ from the old internationalism of *laissez-faire* and the 'invisible hand'.

The Socialism that is needed must be, then, pacifist, internationalist, resistant to the appeal to nationalist fears and passions; but its internationalism must be of a positive, and not merely of a negative, sort. It must aim at re-establishing international trade on a basis of useful exchange by collective planning on a world basis, and not by merely letting things alone. Internally, it must be bold and challenging, and yet—above all—not silly or unscientific; for it has to get the best practical brains in the community as well as the mass of the consumers over to its side. It has to be democratic, and against all undemocratic dictatorships on the Fascist model; but it has also to reinterpret democracy so as to reconcile it with swift and vigorous action, and, in using Parliaments, to use them in new ways appropriate to the new situations with which they are called upon to deal.

For such a Socialism, if it can be made the basis of an effective movement, there is to-day not merely the hope, but the reasonable confidence, of victory. For the world is offered no alternative to it save chaos—though chaos may be staved off for a time by various forms of controlled Capitalism, from Nazism at one extreme to President Roosevelt's Industrial Recovery programme at the other. These alternatives, I have tried to show, are inherently unstable and impermanent: they lead back again to the old unsolved problems of the capitalist system. For the world will not emerge from its troubles until it devises an economic, as well as a financial, system that enables it, by a wide diffusion of consuming power related to a planned distribution of its productive resources, to make use of the means to plenty which the advance of man's power over nature has now put well within its reach.

II

ECONOMICS IN THE MODERN WORLD[1]

The classical theories of Economics and Politics, on which the university students of to-day are still being brought up, were constructed by and for an age of successful individualism. They grew up amid, and were largely based upon, that rapid and uncontrolled expansion of man's power over nature which lies at the root of modern Capitalism, and above all of that phase of it we call the 'Industrial Revolution'. In face of this swift onrush of productive power, the system which men had built up in the past for the collective control of their economic lives came to appear petty and obstructive; and the first duty of the reformer seemed to lie in the clearing away of a mass of ancient rubbish which still impeded the course of economic and political advancement. Bentham, with his sweeping doctrine of Utilitarianism, was the foremost prophet of this destruction. The 'greatest happiness' principle became the powerful solvent of ancient institutions that had turned into current abuses; and in calling upon all men's traditions to justify their life or perish, Bentham and his followers hewed the path for economic and political thought into the nineteenth-century world. Nineteenth-century theory, in both politics and economics, based itself on Bentham; and, though his own work was mainly political and legal, the triumph of his ideas was most complete in the economic field, because there the new forces of which he was the interpreter had their foundations.

In the circumstances of the time, Utilitarianism was bound to take on an individualistic form, though there is nothing essentially individualistic about the Utilitarian principle. The new economic forces were being wielded by

[1] Originally published in the *Political Quarterly*, April-June 1933.

individuals, and such collective forces as existed were for the most part antagonistic to their growth. The struggle for progress appeared as a struggle to escape from the bondage of the old collective controls; and it seemed natural not only to back the individuals who were contending for the power to make full use of the new productive powers, but also to set out to remould political institutions in harmony with the new economic individualism. In economics, the human being was conceived as an individual agent of production, making his impression upon a 'free market' in accordance with the quality of his productive powers. Every man's natural ambition was to become an *entrepreneur*, and no obstacles of law or custom ought to be allowed to stand in his way if he had the requisite personal qualities. Landlords were out of favour, because their power rested on monopoly, and not upon individual initiative. Wage-earners were those who lacked the right to exact monopolistic tribute, or the personal qualities needed for becoming *entrepreneurs*. The *entrepreneur* alone was the self-realising individual—the self-made man—in the fullest sense; and on his enterprise rested the progress of mankind.

A political theory was needed to complement this theory of the economic world. All aristocratic theories were ruled out, because they all involved a foundation of monopolistic privilege. There remained only democracy; and the Benthamites were thoroughgoing democrats in their theoretical outlook. 'One man, one vote' was the only sound political principle, even though such 'fantastic notions' as that of 'natural rights' were flung overboard; for 'one man, one vote' corresponded in politics to the equal right of all to exploit the powers of production to the height of their capacity. It alone would secure that the persons of most political enterprise would get most weight in shaping the affairs of nations.

Parliamentary democracy thus appeared as the logical complement of Capitalism in the economic field, and it became necessary to square the economic survival of the

fittest with the political principle of the greatest happiness of the greatest number. Adam Smith made smooth the way for the conception of an 'economic harmony', whereby each man in pursuing his own interest would be somehow guided to secure that of Society as a whole. On the one hand, it was contended that the freedom of enterprise and trade from all forms of restriction would lead to the maximum total production of wealth, and that higher production would necessarily enlarge the funds available for the remuneration of labour—the famous Wages Fund of the classical economists; and on the other hand, when the Wages Fund was given up, its place was taken by the notion that the higher the productivity of labour the higher would its wages also be. But in addition, as Jevons and other writers hit on the notion that value depended on utility, measured by consumers' demand, rather than on labour or cost or price of production, the conception of the underlying economic harmony was reconstructed in a new form. Each consumer, it was urged, would be as a rule the best judge of what he wanted; and the unfettered freedom of the market, by allowing him to exercise free choice among all the goods and services offered for sale, would automatically maximise satisfactions, in that each consumer would spend his income on what he wanted most, and the scarcity of goods would cut off only the less urgent demands.

This view, of course, rested on an assumption. The Austrians, who were its chief exponents, delighted to show that any individual consumer, having a given income, would clearly spend it to the best advantage he could, and thus tend to get the maximum of satisfaction; and they then proceeded to assume that what was true of any individual consumer must be true of all, and therefore of the market as a whole. This, however, was to ignore the fact that different consumers possessed very different incomes and were, therefore, by no means equally placed for making their several demands effective. Goods in a market tend to sell at a uniform price for any two like products of equal quality; and one shilling in the hands of the poor man has

only the same purchasing power over goods as one shilling in the hands of the rich. It is doubtless true that, as men satisfy first their most urgent needs, the poor man tends to get a higher average satisfaction out of each shilling of his income than the rich; but, if he has far less shillings to spend, he also gets far less total satisfaction, though there is no evidence that his needs or capacities for satisfaction are any less. Accordingly, there is always a presumption that, the nearer the distribution of income in a Society approaches to equality, the higher is the total satisfaction likely to be derived from the goods this income is used to buy. Inequality is therefore defensible on Benthamite principles only to the extent to which it can be shown to be necessary in order to maximise the total of wealth produced. It can be at best only a necessary evil; and maximum production with unequal distribution *may* result in less total welfare than a smaller product more evenly distributed.

Nor is this all. Many economists have recognised the unequal marginal utility of money to different purchasers, and yet have clung to the opinion that the 'free market' is somehow a guarantee of maximum welfare. But it is evident that this view, if it is put forward *a priori*, depends on an unwarrantable identification of want with demand, whereas the economic system in fact takes no cognisance of wants unless they appear in the market in the form of effective demand. The theory, favoured by Jevons and the Austrians, and by the *laissez-faire* revivalists of our own day, that prices depend on demand conditions, which are then identified with 'utility', is doubly false. It is false because there is no necessary coincidence of utility with demand, and it is false because it assumes the independent existence of incomes apart from the productive process.

If once the economist is allowed to begin by assuming this independent existence of incomes, he will find no difficulty in building upon this assumption a perfectly logical case in support of the view that prices depend upon

demand, though even so he will not be able to prove that the satisfaction of the highest price-offers is any guarantee of the highest possible total of human welfare or satisfaction. But it is preposterous to grant him this assumption, in face of the fact that incomes are actually generated in the productive process. It is easy enough to demonstrate the logical priority of want over supply; for it is clearly absurd to produce goods unless they are wanted. But this in no way shows that demand is prior to, or governs, supply; for want and demand are not the same thing. Wants are—just wants, whereas demand is want armed with an income—with a supply of purchasing power.

It cannot therefore be legitimate to assume the existence of demand as the starting-point of economic analysis, unless the conditions which create demand are also assumed. And it cannot be irrelevant, if we are to take account of demand, to enquire into the origin of the incomes which convert want into demand. But as soon as we do embark on this enquiry, the beautiful simplicity of the Austrian doctrine is destroyed; for it has to be admitted that demand, so far from being itself the sole cause of production, is itself produced in the course of production, and that the magnitude and the direction of the demand existing at any time depend alike on the scale on which production is being carried on, and on the proportions in which incomes are being distributed in the productive system, or redistributed subsequently by levies upon the incomes generated in the course of production.

This is, of course, admitted up to a point; but, having admitted it, the adherents of the 'demand' school fall back on their second line of defence. Within the productive system, each factor of production is paid for in accordance with its 'marginal productivity', that is to say, broadly, at a price corresponding to the value contributed by the last unit of it that is actually employed. The location of the marginal point for each factor is set, we are told, by the conditions of consumers' demand; for the intermediate demand for all the factors of production is derived from the

demand for consumers' goods and services. The consumers are willing to pay so much or so much, according to the quantity placed on the market, and in accordance with the varying marginal utility of the commodity to themselves. What they are willing to pay has to be divided out among the factors of production; and the division will be decided by the competition between the factors to secure employment, on terms which will inexorably make the remuneration of each factor coincide with its marginal productivity.

Now, this looks very like a true picture of what happens. For, if we look at the economic world at any particular moment, incomes do exist, and do make up a total of composite demand in accordance with the preferences of buyers; and the demands of final consumers are reacting upon the productive system so as to cause changes in the demand for, and the prices offered for, every factor of production, from the various kinds of labour and materials to machines, insurances, and borrowed or invested capital. If we once assume the incomes, or even take them as we find them in the market at a particular time, all the rest seems to follow logically.

But we cannot do this; for it is equally true and relevant that the production, and the distribution of incomes which goes with it, is the source of the demand. The incomes cannot exist until production has taken place, any more than production can go on in the absence of incomes to purchase the product. In effect, the abstract method of starting with a single aspect of the economic system, and then deriving the rest from it, will not do. The system hangs together, as a system. All its aspects exist together, and the relation between them is one, not of cause and effect, but of mutual determination.

This, however, may be held to have nothing to do with individualism. In my view, it has a great deal. The abstract method is essentially atomistic. It tries to lead us to an understanding of the economic world by a separate analysis of its parts, and above all by basing this analysis on a supposedly typical sample. We are asked to begin by studying

the behaviour of a typical business man reacting to the typical consumer's demand. That the consumer and the business man, and the behaviour of both, are correctly described does not mean, unhappily, that we have been brought any nearer to an understanding of the system within which they both exist. For their behaviour is a reaction to the system, and would be quite different in many respects if the system were changed.

The object of the advocates of *laissez-faire* is to show that there exists, in any organised economic Society, a possibility of equilibrium, and a tendency for equilibrium to be actually realised if economic forces are left 'free'. Thus, it is assumed that, if the consumers possess a certain income, and distribute that income in accordance with the principles of utility, there follows inexorably a certain set of prices at which all the available factors of production will be able to be fully employed. If, then, unemployment of any factor actually exists, this is a sign of disequilibrium, which must be the result (unless it is a mere passing effect of friction due to economic change) of obstructive forces which are somehow keeping the prices of certain things unduly high. The high prices may arise from *entrepreneur* monopoly, Trade Union pressure, or social legislation, or others forms of interference with the law of the free market; but it is assumed that there must be for everything an equilibrium price, at which the available stock will be fully absorbed.

This would be perfectly true, if incomes and their distribution were unaffected by changes in the prices of the factors of production. But in reality these prices are incomes, or constituents of incomes, and no change can take place in any of them without affecting the character of demand. There *may* be a level of prices for all the factors of production at which all these factors will be employed to the full. But there may be no such level, within the existing industrial system. For if high wages or interest rates can cause unemployment by making production unprofitable to the *entrepreneur*, low interest rates can so check the

accumulation of capital, and low wages so depress the level of consumers' demand for ordinary consumption-goods, as to have the same result. Nor is there necessarily a right wage or interest rate between these two at which full employment of resources will be secured. For the system of prices which will enable *entrepreneurs* to employ all the resources at the existing level, and with the existing distribution of incomes, may introduce such changes into the level and distribution of incomes as again to upset the balance.

The presumption in favour of *laissez-faire* as a means of preventing unemployment and ensuring maximum production cannot therefore be sustained. If we want to establish a balance involving the full use of productive resources, we shall have to establish it by the co-ordinated control of the factors concerned, and not by allowing prices (and therefore incomes) to find their own level. This is not because there is, as some people have supposed, any inherent tendency in the present economic system towards a deficiency of purchasing power in relation to the actual volume of current production; for, save as an occasional accompaniment of banking deflation, no such tendency exists. It is rather because the distribution of incomes, rather than their aggregate amount, constitutes the vital factor. In order to secure full employment, incomes must be so distributed that the demand arising from them coincides with the power of the productive system to supply the various types of goods and services, and equally the productive system must be constantly adjusted to fit in with the demands arising out of the actual distribution of incomes. If the double adjustment could be successfully made, unemployment as more than a matter of friction would disappear. But we cannot rely on the adjustment being made automatically, when the factors are left uncontrolled. For the attempt to get equilibrium in one field will always tend to upset equilibrium elsewhere.

In plain fact, the mechanism of modern capitalist Society is not self-adjusting. But the truth goes deeper than this;

for in economics, as in politics, the forces upon which it rests are not isolated individuals exchanging goods in a market which is simply a place of meeting for many individual buyers and sellers, but groups, institutions, associations, and classes which cohere in varying degrees, and by their cohesion shape the conditions of exchange. What is called monopoly is not an occasional and exceptional interference with the working of a market normally 'free', but an omnipresent condition varying in strength and degree from case to case. Production is not, in such a system, a mere response to demand, though it is limited by what consumers can be persuaded to buy; for the persuasion of consumers by suggestion and advertisement forms an integral part of the productive system, and the *entrepreneurs*, by their control of prices, fix the limits of demand fully as often as they leave the conditions of demand to fix the price. Consumers' demand, again, is not a thing existing absolutely, but rather a response to an existing structure of prices constantly modified by changes in the distribution of incomes through production, as well as by the acts of the producers in devising new goods and new methods of production, and in influencing the direction of demand through various forms of propaganda. The trader, mediating between producers and consumers, is influenced fully as much by changes in the conditions of supply as by the changing tastes of the consumers. And finally, though consumers' purchases are still for the most part made individually, or by households, demand tends to go by groups and classes, according to social fashions and conventions of living, rather than by the personal valuations of individual consumers. The producer standardises supply in order to lower costs by mass production; and the consumer is led to standardise demand, not only as a means to cheapness, but also as a response to the producers' suggestions and the traders' stocking of standard lines.

This collectivisation of the market, on the sides of production and consumption alike, progressively restricts the range of individual action, and makes obsolete all analyses

of the economic situation conceived in *laissez-faire* terms. In these circumstances, the hankering after *laissez-faire* is mere inverted Utopianism—a wish for a different economic system belonging to the past, and not for an improvement in the working of the productive system of to-day. For it is not *laissez-faire* to be governed by the contentions of a large number of imperfect and sectional monopolies; but this is the only possible consequence in the world of to-day of a refusal to use the State as an instrument of economic regulation. The source of our present troubles is not that States interfere too much, but that their interference remains external and mainly negative. Being external and negative, this interference is as liable as any other sectional and limited control to lead to disequilibrium; for it lacks the power to balance one act of intervention by others designed to bring the rest of the system into the right adjustment. States, when they have interfered of late years, have so often made a mess of things that it is tempting to conclude that they should not interfere at all. But they have interfered, for the most part, not because their governments wished to do so—on the contrary most governments have a strong theoretical bias in favour of letting industry alone—but because they have been irresistibly driven to interfere, in order to correct maladjustments which have arisen out of the working of the system itself.

The most profound of these maladjustments arise from the present transitional organisation of the productive process. In a simple Society of individual producers, goods are brought to market and sold for what they will fetch, and their prices in terms of other goods determine the standards of life of the various producers. All incomes are the direct outcome of selling goods in the market, and every expectation of earning an income acts directly as an incentive to production. But in the modern system, based on the hire of capital and labour by a special class of *entrepreneurs* acting on behalf of a wider body of shareholders, this is not the case. Only *entrepreneurs'* and shareholders' expectations of income act as incentives to production in an unqualified

sense: other incomes, those of creditors and wage- and salary-earners, act also as deterrents, because they appear as costs reducing the net expectations of the *entrepreneurs* and the shareholders. It is true that these latter incomes are essential for the purchase of the product, and do serve as incentives to that extent. But the sums paid out in wages and salaries can only be recovered by the sale of the product, whereas the sums paid out as profits represent a demand not balanced by outgoings, and to maximise these is accordingly the object of the *entrepreneur*. Wages, interest, and profits are all alike incomes, forms of purchasing power to be recovered by the sale of the products of industry. But wages and interest (and also rents) are balanced by outgoings, and appear as deterrents to production because any rise in them threatens to reduce the margin between cost and selling price.

Thus, whereas a community of independent producers would be in no wise tempted to reduce production because of a fall in prices, a capitalist community is at once tempted to react in this way, in order to escape the burden of wages and interest. And, if once production is reduced in this fashion, the result is to cancel incomes as well as products, and to cause supply and demand again to approach a balance at a lower level. There is accordingly no necessary reason why a factor of production once disemployed should ever be re-employed, or why depression should not be self-perpetuating. In fact, if reliance were placed solely on the internal rhythm of the economic system itself, apart from forces arising outside the circle of depression or from deliberate reflationary action within it, there is no necessary reason why any slump should ever end. Production and consumption can balance, subject to secondary friction, at any level of activity. The most perfect balance would be achieved if production stopped altogether, and all the consumers were dead.

This being so, our analysis of the modern economic system must take full account, not only of the relations of incomes as a whole to production as well as to consumption,

or of the effects of varying distributions of incomes on consumers' demand, but also of the differences between those incomes which constitute costs, and therefore deterrents to production, and those which, arising out of a surplus of price over cost, constitute incentives to production. It matters to the determination of the level of productive activity, not only in what relative magnitudes incomes are distributed, but also in what forms. And any Society in which some incomes are also costs, whereas others are not, is bound to be liable to that kind of disequilibrium which appears in the unemployment of productive resources.

The remedy is to convert all incomes back to the form which they possessed when the economic system was carried on by independent producers, but to do this in a new way based on the collective character of the modern process of production. It is to make the national income a national dividend, that is to say, a claim on the part of every citizen to a certain share in the total supply of goods and services that can be made available for consumption. This is compatible with the existence of fixed money claims, such as wages and salaries or interest or rents, only if the community, by a collective control over prices, is in a position to adjust the purchasing value of these fixed money claims so as to equate them to the supply of goods and services that can be made available. In the alternative, if prices are to be left free to vary uncontrolled, all forms of income must be variable too, or else the balance of production and demand will be lost. But variable prices and variable incomes together are not consistent with any effective planning of the use of productive resources: so we are compelled to rely, as a means of maximising the utilisation of these resources, on a careful and co-ordinated adjustment of incomes and selling prices at the levels necessary to secure this result.

Thus, in the economic sphere, the partial monopolies characteristic of modern production lead on to socialisation; and the tendencies to disequilibrium arising from the unequal pulls of conflicting groups and classes can be over-

come only by the supersession of these sectional forces by an inclusive public monopoly. Similarly, in the political sphere, it is futile to analyse the forces of to-day in terms of individual citizens, or voters, or as if the candidate appeared before the electors simply as an individual political *entrepreneur*, appealing on the strength of his personal qualities. For in fact the electors are arranged in groups, classes, interests, acting together under the stress of collective incentives and desires; and candidates stand for parties, which are the embodiment of wider or narrower collections of policies based on these same divisions among men. Any political theory which ignores these collective realities is utterly meaningless and unrealistic; and, once again, the only way in which the conflict of sectional interests can be transcended is by merging the rival groups in a wider collective unity. Politics, as well as economics, stands in need of socialisation; but, as political groups are mainly, though not wholly, the reflection of economic classes and interests, the transformation of politics can in fact only follow, and not precede, the socialisation of the economic life of the community.

Meanwhile, to study realistically the facts of to-day and the tendencies which are shaping the future, we must think in terms, not of typical individuals, but of the strength and influence of the contending collective forces. For economic and political analyses are alike of value only if they are at once truly descriptive of current facts, and—what is really the same thing—revealing of the tendencies which are driving us forward to the next stage of social development. For tendencies are facts, more really and fundamentally matters of fact than abstractions which are conceived in static terms. If there is such a thing as equilibrium, in either politics or economics, it must be a dynamic and not a static equilibrium. Finally, we must above all avoid abstract reasonings based on the conception of the individual citizen, or consumer or producer, as the determining force in political or economic affairs, and must learn to think rather in terms of constantly developing and interrelated groups

as giving form and substance to the activities of the individual. Economics and politics, in these dynamic forms, may be harder both to teach and to learn than the hallowed formulæ of the individualist schools. But a science is not the better for being easy, if in order to simplify its problems it consents to distort the truth.

III

A NOTE ON *LAISSEZ-FAIRE*[1]

Any attempt to write a historical account of the doctrine of *laissez-faire* would almost involve the writing of a complete history of 'orthodox' economic theories, at any rate from the days of the French Physiocrats to the middle of the nineteenth century. For classical economic theory, as it developed especially in Great Britain under the influence of Adam Smith, was based throughout on the underlying idea of *laissez-faire* as the logical corollary of the division of labour which Adam Smith analysed in his famous opening chapter. This underlying idea is above all that the economic affairs of Society can in the main be relied upon to take care of themselves if neither the State nor any other body armed with coercive authority attempts to interfere with their working, and if they are left entirely under the influence of the individual activities of men. This view in turn depends on an optimistic opinion about the nature of the universe, and implies the conception of a 'natural order' or system of economic harmonies which is bound to prevail and work out to mankind's advantage in the absence of positive regulation.

For the purpose of this brief comment upon the doctrine it is unnecessary to give more than a very general indication of the stages by which it thus rose for a time to a position of almost undisputed pre-eminence among economic writers. It would be quite possible to trace back the history of *laissez-faire* notions a very long way, and to find anticipations of them, especially among the earlier Italian economists such as Serra in the seventeenth century. But there is no need for my present purpose to go

[1] Based on an article written for the *Encyclopaedia of the Social Sciences*.

back further than the supposed origin of the phrase itself in eighteenth-century France. The first use of the maxim '*laissez-faire, laissez-passer*' has been commonly attributed to Gournay (1712–1759), at first a merchant and later one of the 'intendants' of commerce and a friend of Turgot. But Turgot himself in his *Éloge* of Gournay ascribes the phrase '*laissons-nous faire*' to another merchant, Legendre, who is said to have used it in pressing upon Colbert the desire of the mercantile community that the State should let them alone. D'Argenson has also been sometimes credited with the invention of the maxim; but Gournay, even if he did not originate the phrase, seems to have amplified and popularised it in the longer form, '*laissez-faire, laissez-passer*'; and it became in the latter part of the eighteenth century, sometimes in one form and sometimes in another, a common expression among writers of the Physiocratic School and those nearly allied to them in thought and doctrine. Adam Smith adopted from the Physiocrats the underlying idea, though not the phrase, which did not itself become widely current in England until John Stuart Mill used it in the title of one of the sections of his *Principles of Political Economy* in 1848. Since then it has come to be most closely associated in people's minds with the doctrines of the so-called 'Manchester School' in England, and especially with the opposition to any extension of State intervention in industry through such measures as Factory Acts or the public regulation of industry, and above all in the sphere of commercial policy with the advocacy of Free Trade. In this latter connection the word 'Cobdenism' has often been used as practically equivalent to *laissez-faire*. On the other hand, among Continental economists *laissez-faire* ideas are now most closely connected in people's minds with the Austrian School, with whom the *laissez-faire* principle, though it involves the same practical consequences as the Manchester School doctrine in Great Britain, is linked up more directly with a particular set of assumptions used as the basis for the working out of an

abstract economic theory, which has then to be applied to the real world by removing or modifying one by one the assumptions on which it is founded.

The *laissez-faire* doctrine, in the form in which it was held by the Physiocrats in eighteenth-century France, was in the first place and most directly the expression of a protest against the vexatious system of public regulation then encompassing industry under what is often called 'Colbertism'; but it was also in a deeper sense the outcome of the view that as only agriculture is truly productive and manufacture and commerce are unable to create wealth and can only serve as means of distributing wealth already in existence, taxes ought to be levied on land and not on industry or commerce, which should be left free to pursue their mission of distributing wealth without interference by the State. This seemed to the Physiocrats the 'natural' arrangement; and their conception of a 'natural order' underlying the actual operation of economic affairs was developed much further by Adam Smith. It is indeed in *The Wealth of Nations* that there emerges clearly the doctrine of a 'natural harmony' which somehow ensures that each man, in pursuing his own economic interests, will be mysteriously guided to further the interests of all. This view is obviously connected very closely in Adam Smith's mind with the assumption that any money which comes into the hands of the State by way of taxation is practically certain to be spent unproductively and not in such a way as to further the development of economic enterprise. It is significant that the treatment of the problem of taxation and public debts in *The Wealth of Nations* takes no account of the possibility, admitted by even the most individualistic of modern economic writers, that money in the hands of the State can be put to productive as well as to unproductive use. Adam Smith was too much obsessed by his ever-present vision of the mounting National Debt and by his sense of the actually restrictive and anti-social tendencies of State intervention in his own day, ever to realise the

possibilities of productive State expenditure in the general interest. Nor is this in the least surprising; for just as Bentham was led from a different angle to a denunciation of all kinds of privileged corporation and monopoly and to a declaration of faith in complete political as well as economic *laissez-faire* by his sense of the unhappiness caused by the numerous privileged institutions which he saw everywhere around him, so Adam Smith, confining his observation more strictly to the economic field, found it hard to discover any institution at all in which the class State of the eighteenth century, whatever its motives, was actually so intervening in economic matters as to promote the wealth of nations.

We thus get in Adam Smith's writings the outline of an economic theory founded essentially upon individualism. The source of wealth for nations is held to lie solely in efforts made by individuals, in the use which they make of the factors of production—land, labour, and capital—which are at their disposal, and in their success in producing 'use values', which are also exchange values, under the inducement of a prospect of economic reward. It is not suggested by Adam Smith that every man is perfectly enlightened in this pursuit, or for that matter that every man is perfectly selfish, for the classical economic doctrine does not postulate the 'economic man' in the sense sometimes attributed to it. It is, however, suggested that all the individuals acting independently one of another are likely to be better judges than any collective body can be of the means of producing the maximum amount of wealth. It is almost an axiom with Adam Smith, again derived from observation of contemporary affairs, that men are sluggish and unenterprising in their management of collective concerns, and that only the individual paddling his own canoe can be relied on to show the requisite qualities for making the best use of the factors of production. Hence comes Adam Smith's profound distrust, which he shared with eighteenth-century legislators, of the joint stock company as a form of industrial organisation, except for a limited

range of enterprises that are capable of being reduced for the most part to a simple and invariable routine. Adam Smith believes that the individual in pursuit of his own gain will set out to produce as much utility as he possibly can, and will be driven by the force of competition to do this as a condition of survival and success in business either as an employer or as an employee. The sum of the efforts of all the individuals to create the greatest possible amount of wealth will thus result, if they are allowed to follow each his own bent, in the creation of the maximum amount of wealth in Society as a whole. This will come about because of the existence of a 'natural order' in which the interests of the individuals are harmonised with the good of Society as a whole; and interference with the free working of this 'natural order', though it may be justified in exceptional instances on *non-economic* grounds, as in the case of the Navigation Laws, is bound in Adam Smith's view to diminish the sum-total of wealth produced. Thus all forms of State intervention for the purpose of regulating commerce so as to produce an influx of the precious metals or a 'favourable balance of trade' must have the effect of diminishing the total wealth of the world by diverting trade and production from the channels along which they would 'naturally' flow into others which individuals left to their own devices would reject as less productive on grounds of enlightened self-interest.

This conception of a 'natural order' and a 'natural harmony', based on what the order of the universe will cause human nature to do if it is left to its own devices, pervades and underlies not only the writings of Adam Smith, but often in a less conscious way those of the classical economists of the late eighteenth and early nineteenth centuries. It receives, moreover, a philosophical reinforcement from the teaching of Bentham and his Utilitarian successors. For the philosophical doctrine which erects pleasure as the sole end of human action, and makes each man the only competent judge of his own pleasure, fits in exactly with the notion that each man is the best

judge of his own economic interest. He pursues his economic interest as a means to pleasure, and as pleasure is regarded as essentially quantitative, and the 'pleasure of society' as merely the sum of the individual pleasures enjoyed by its members, that course which most furthers these individual pleasures must also tend to the realisation of the maximum of social pleasure or social utility. This Benthamite doctrine was destined to be turned to very different uses at a later stage; but in the England of the early nineteenth century it became the immensely influential philosophic ally of the *laissez-faire* doctrine in the economic field. The economic good of Society came to be regarded, like the pleasure or happiness of Society, as the sum-total of the goods accruing to all the separate individuals of whom Society is made up.

In Adam Smith and his successors up to John Stuart Mill the theory of value was, of course, based mainly on a consideration of the forces and factors of production. Value was conceived as depending upon and determined by the quantity of labour, or sometimes by the quantities of labour, capital, and land embodied in a commodity, or alternatively by the money cost of producing the commodity—its 'price of production', to use Mill's phrase—which was regarded as constant for the quantities of the factors of production used up in making it. This view of the process of value-creation put the emphasis on the rewards meted out to the various factors of production, and regarded these rewards as necessary inducements to produce as much as possible. The rewards or incomes accruing to the owners of the factors of production consisted, however, fundamentally not of sums of money but of the goods which these sums of money could be used to buy; and from the time of Stanley Jevons the emphasis in the formulation of the theory of value was shifted over from the side of production or supply to that of demand. Jevons repudiated Adam Smith's distinction between 'value in use' and 'value in exchange', which the earlier economists had regarded as fundamental, and set out to measure the value of goods not by measuring their cost of

production or the amounts of the factors of production incorporated in them, but primarily in terms of the amounts of utility which they embodied, that is to say, their capacity to yield pleasure or satisfaction to the consumer. Production came to be thought of as a response to the economic stimulus of consumers' demand; and consumers' demand came to be thought of as inducing the producers to supply those goods which would yield the maximum total of satisfaction.

Under the new theories formulated in England by Stanley Jevons and developed on the Continent especially by the Austrian school (Menger, Böhm-Bawerk, etc.), the doctrine of *laissez-faire* acquired a new sanction. Free consumers' demand, regarded as the omnipotent force which would govern supply in the absence of artificial restrictions, came to be treated as the guarantee of maximum production of wealth and satisfaction; and State intervention was looked on as bad because it necessarily interfered with the free expression of consumers' demand by altering the conditions of supply and price. It is in these terms, vitally different from those of Adam Smith and Ricardo, that the doctrine of *laissez-faire* is put forward to-day where it is still put forward at all, as it still is to a surprising extent among academic economists. Emphasis is placed no longer on the self-interest of each producer as making for the maximum production of economic values, but rather on the assurance given by the free play of consumers' demand under a competitive system that the production of goods and services will be such as to create the maximum sum-total of human satisfactions.

Economists who advocate *laissez-faire* doctrines to-day usually state their case mainly on this ground. They urge the necessity for allowing the freest possible play of consumers' demand as a means of securing maximum utility in opposition to any attempt by the State or by any other body such as a trade combine or a Trade Union to fix or influence the prices of commodities or services, including the service of human labour. Only in popular economics

does the older argument that each producer in seeking his own advantage is led by the operation of an 'invisible hand' to promote the advantage of Society as a whole still play any important part. In popular economics this contention is still prevalent, and the unquestioned assumption that this will happen is still very commonly made, especially among business men. But it would be difficult to find much sanction for it in the theories of modern economists.

The conception of the 'order of nature' and the 'natural economic harmony', so dear to Bastiat and to the Free Traders of the mid-nineteenth century as well as to their predecessors of the Classical School, thus assumes a new form. But it remains essentially Benthamite, or rather Utilitarian. For its basis now is that the consumer is the best judge of his own satisfactions, and that these are measured under conditions of *laissez-faire* by the prices which he is prepared to offer for the various goods put forward for sale. Bentham's calculus of pleasures and Bentham's doctrine that 'pushpin is as good as poetry' find economic expression in the price offers of the consuming public. Satisfaction is to be measured simply by demand price; or at all events the economist is concerned only with satisfactions that can be measured in this way.

But, as Marshall and many other economists have pointed out, the case for *laissez-faire*, when it is presented in this form, cannot stand examination. For the price-offers made by the consumers depend not only on the amounts of satisfaction which they expect to get from their purchases but also on the size of their incomes. If incomes are unequal then equal price-offers are not measures of equal satisfactions expected; and there is accordingly no reason for supposing that a system which relies exclusively on the free play of consumers' demand will result in the maximum sum-total of satisfactions. Bentham's other principle, the greatest happiness of the greatest number, can be successfully invoked against any such facile conclusion; for the greatest happiness of the greatest number might evidently be better promoted by a different distribution of

wealth, which would result in a quite different series of price-offers being made by the consumers.

The case for *laissez-faire* thus breaks down in one of its aspects, and the Utilitarian principle originally invoked against State interference becomes an argument in favour of forms of State intervention designed to lessen the inequalities of income in order to promote a greater sum-total of satisfaction. This constitutes the essential case against *laissez-faire* in such matters as the State regulation of wages through legislation setting up a minimum wage, or the use of taxation with the deliberate object of bringing about a redistribution of incomes. Moreover, the same Benthamite principle of the greatest happiness of the greatest number provides a case for factory legislation and other forms of State intervention designed to remove occasions of unhappiness which arise out of the system of 'free contract' between employer and employed.

But it can still be argued that, even if the State ought, in the interest of the greatest happiness of the greatest number, to interfere with the distribution of incomes, it ought not to interfere with the pricing of commodities, on the ground that each consumer is the best judge of what he wants, and that, given a satisfactory distribution of incomes within the community, the free play of consumers' demand can be relied on to lead to the production of the maximum total of utility. Hardly anyone, however, would be prepared to push this principle to the extreme point, for it will be agreed that the State is reasonably entitled to tax certain types of luxury goods and services, especially such as are harmful if consumed to excess, and thus raise their prices to the consumer. Nor will many people deny that the State can reasonably intervene to provide or ensure the provision of certain things at specially low prices where it desires for social reasons to increase their consumption. Alcoholic liquors are a familiar instance of the former, and water of the latter type of commodity. But such instances are commonly regarded as exceptional, and many people still hold that over the greater part of

the field consumers' demand ought to be given free play in order that its expression in demand prices may stimulate the maximum output of satisfactions.

In the international sphere this idea lies at the root of the traditional case for Free Trade. Tariffs or other forms of Protection are held to constitute an arbitrary interference with the free play of consumers' demand, and to tend for this reason to reduce the total of satisfactions. Free Trade is only a corollary of the doctrine which makes consumers' demand the most suitable final arbiter of prices and production.

But in the circumstances of the modern world this view of the actual working of the price system can hardly be sustained. For under the modern conditions of increasing combination among producers of almost every type, price-fixing has become more and more a function of production rather than of demand. It is of course perfectly true that the producer has in the nature of the case to work within limits set by consumers' demand. But this demand does not fix the prices to be charged, but only settles what quantities can be sold at any given price level, and thus presents the producers with a number of alternative price levels at which they can expect to dispose of varying quantities of goods. In these circumstances the producers in fact more and more fix the actual prices, either directly or by adjusting the quantities of goods which they place on the market to their knowledge of the state of consumers' demand. They can of course do this only where some degree of formal or informal combination exists among them. But combination strong enough to make this possible has become so common as to be rather the rule than the exception in industry to-day.

The advocates of *laissez-faire* were opposed not only to State intervention, but also to all forms of private combination which are designed to influence prices, since they held that these always tend to decrease the total utilities produced by the economic system. But the efforts of believers in *laissez-faire* to prevent combination by means

of anti-trust legislation or by the restriction of monopoly prices have either failed, or have themselves involved the negation of the *laissez-faire* doctrine by calling for an extension of State intervention in order to counteract the influence of private combination. It has now been discovered that combinations among producers cannot under modern conditions be prevented, but only at most regulated and controlled. Preventive measures merely fail; and regulative measures necessarily involve an abandonment of *laissez-faire*. Combination has therefore to be accepted by modern advocates of *laissez-faire* as an inevitable element in the system of private enterprise under modern conditions; and those who still advocate *laissez-faire* in the sense of an absence of State intervention come to mean in practice by *laissez-faire* not an absence of combination, but the fullest freedom of action for it. The price system, if it is not regulated by the State, comes to be governed not by consumers' demand as a single force, but more and more by the combined producers acting within the limits set by consumers' demand. But prices fixed in this way can no longer be regarded as a part of the order of nature, or as having any inherent tendency to promote the maximum total of satisfactions.

Therefore at this point too the familiar case for *laissez-faire* breaks down in face of the transformation of the modern capitalist system from unregulated to regulated production. The tendency in modern industry is not only towards a tariff policy based on partly economic and partly non-economic conceptions of Economic Nationalism, but also towards the building up both by national units and across national frontiers of large industrial combines and concerns strong enough to exert a considerable measure of control over both prices and output, and therefore creating a new case both for State intervention and for regulation transcending national limits. The German cartel system and the measures taken by the German State to control the prices charged by the cartels furnish, especially in their most recent developments under the Nazi régime, an out-

standing example of this tendency within a single country, and only the absence of any international authority capable of exerting control over a wider field has prevented the growth of a demand for international forms of regulation, which can indeed be seen as adumbrated in the deliberations of many of the sub-committees of the abortive World Economic Conference of 1933.

This growth of large-scale organisation through powerful industrial and trading combines, and the necessity for public control which arises out of it, obviously lead in the direction of Socialism; and the opponents of Socialism, unable to rest a defensible case for *laissez-faire* on the old grounds of consumers' freedom, are now inclined to slip back to advocating it on the grounds that it leads to efficiency in production and is the only means of providing producers with a sufficient incentive to do their best. It is no longer quite maintained that there exists the 'pre-established harmony' which causes the pursuit by each individual of his own self-interest to result in the well-being of all; but it is argued that unless each man and each business unit are left free to profit by their own exertions without having their activities hampered by the intervention of the State, there will be no incentive strong enough to get the world's productive resources adequately developed. This argument is most commonly advanced against Socialism—that is, against any system under which industry would be collectively owned and conducted, and the profit incentive removed—but it is often also used as a reason for keeping State interference with privately conducted industry down to a minimum, and also as an argument against any heavy taxation of profits imposed for the purpose of promoting the redistribution of incomes.

In effect, however, under the conditions of large-scale industrialism, especially in the older industrial countries, the actual conduct of productive enterprise tends to pass more and more into the hands of salaried managers, and the incentive of profit comes to operate directly not upon those who control the actual processes of production, but

rather upon those who have capital to invest. The case for *laissez-faire* thus comes to be reconstituted largely as a case for endeavouring to stimulate investment by allowing an adequate incentive of profit to the owners of stocks or shares. In this form it provokes the Socialist answer that if capital belonged to the community and the processes of investment were accordingly taken out of individual hands and effectively socialised, the incentive of profit would become altogether unnecessary. The advocates of private enterprise and of *laissez-faire* retort that, under such conditions, no more than the dead level of mediocrity will be secured at best, and that both the rewards of enterprise and the penalties imposed on laziness and inefficiency under the profit system are indispensable to the efficient conduct of the process of production. To this the Socialists reply that a communal basis of collective ownership and investment would be able in the sphere of actual productive operations to appeal to new motives of service and to create a new corporate spirit in favour of doing one's best, which would be more than sufficient to replace the dying incentives of pecuniary gain to the employer or investor, and fear of unemployment to the employee.

The argument thus often becomes at this point an argument about 'human nature'. But it is at bottom not so much about 'human nature' as about the forms of organisation and control that are appropriate to the contemporary condition of the powers of production which are available for the use of men. The doctrine of *laissez-faire* grew up and flourished in the nineteenth century first as a reaction against earlier systems of regulation by States and Gilds which had become obstructive and oppressive in relation to the later development of the powers of production, and secondly as the outcome of a conviction that these powers would, at the stage then reached, be most rapidly and thoroughly developed if individuals were left as free as possible to make what use of them they chose.

The suffering to which this freedom for private enterprise gave occasion led speedily to the beginning of the

development of a new system of State regulation through Factory Acts and similar measures, as well as to a more gradual growth of social legislation designed in some degree to redress the more glaring inequalities of incomes. But for some time these new forms of State intervention remained external to the actual conduct of industry, and the State confined itself to the laying down of conditions to which private enterprise had to conform.

Private enterprise was, however, in the latter part of the nineteenth century, radically changing its essential character as the technical revolution made further advances. For the growth in the scale of business organisation was weakening the economic power of the consumer, whereas the growth of democracy was adding to his political power. This situation led inevitably to a demand that political power should be applied to the *positive* promotion of economic ends—which was precisely what the advocates of *laissez-faire* had been above all else concerned to deny. Cobden and Bright, of course, wanted as much as anyone else to use the power of political democracy, in the restricted form in which it existed in their day, for economic ends; but they thought of these ends as essentially *negative* and not *positive*—as the removal of hindrances to the free working of the economic system and not as involving any positive assumption of control over it by the political power. But in practice this distinction could not be sustained when once economic power had become organised and appeared in the market no longer as a natural force but in the form of a conscious control exercised over the market by the organisers of production. Modern large-scale industrialism irretrievably destroyed the theoretical basis of the *laissez-faire* doctrine, as well as its political practicability under the democratic parliamentary system.

Nevertheless *laissez-faire*, discredited as a doctrine and unworkable as a policy in any modern parliamentary State, has still a powerful following. For except among Socialists it still remains in existence as a general presumption, however many particular exceptions to it may

be admitted as inevitable; and each exception has still to be justified by positive arguments against a strong body of opinion which still regards State intervention in economic affairs as in some vague sense 'unnatural' and undesirable on *a priori* grounds. Nor is this surprising; for *laissez-faire* established itself firmly in men's minds as the basis of nineteenth-century industrialism, and all the forces of economic conservatism in the modern world are therefore ranged on its side, as they were in the days of Bentham and Adam Smith on the side of the old regulative system which the economists and Utilitarians were then setting out to destroy. Theoretically developed because the very forms of modern industrial organisation constitute a denial of its first premises, *laissez-faire* still fights in every capitalist country a vigorous rearguard action. The war, however, did much to undermine its traditional influence, for war conditions led to a great increase both in the degree and extent of combination among producers and in the amount of State regulation over industry; and the war also left behind it a situation which compelled States, whether they liked it or not, to perpetuate their intervention, and by promoting the growth of nationalist ideas, fostered the conception of national economies closely linked up with the national State. This conception made its appearance to some extent in every country, even in the planning of the Russian Communists, despite their internationalist ideas, and it has reached the highest point of all in the 'national idea' proclaimed by Italian Fascism and in later variations on the notion of the Corporative State in Germany and elsewhere. The same idea in a less developed form is at the back of the many projects of national planning which, largely under the influence of the Russian example, are now being put forward even by anti-Socialists all over the world. The old attempt to establish a clear line of demarcation between economic and political affairs, on which the doctrine of *laissez-faire* rested, is not merely *démodé*, but absolutely impracticable in the world of to-day. The attempt to use

political power for the promotion of economic ends is universal; and although this development does not settle the question whether Socialism or Capitalism is the better system—for the Corporative State is at one with Socialism in rejecting *laissez-faire*—it does render impossible the basing of the case for Capitalism on the idea of a sharp separation of functions between the economic and the political orders. It thus excludes the *laissez-faire* doctrine, for *laissez-faire* rests essentially on the advocacy of a system of individualism and 'free' capitalist competition. Capitalism, however, cannot be individualistic to-day, and has long ceased to extol competition as its ideal. As a prejudice *laissez-faire* survives, and still wields great power; as a doctrine deserving of theoretical respect in relation to contemporary affairs it is as dead as mutton.

IV

INDUSTRIALISM [1]

Every age and every people has a character stamped upon it by the way it gets its bread. This is true not only of the modern era, which has been called the Age of Industrialism, but of all eras from the beginning of man's time on earth. It is as true of prehistoric peoples or of the Ancient World as of modern Britain or the United States. Modern industrialism does not create man's dependence on his means of living, or first cause Society to take a shape governed by the nature of men's economic activities. It only sets a new shape in place of the old, and causes Societies to organise themselves in different ways.

Industrialism represents, essentially, a particular stage in human knowledge and in man's command over nature—a stage at which man has learnt the arts of machine-production and the use of mechanical power on a large scale, but has not yet become so much the master of these new arts as to bring them to full maturity or under fully satisfactory control. It is a phase in material progress, but only a phase; destined to be superseded when its development has become sufficiently complete. For who can reasonably doubt that, in due time, the world will have so thoroughly solved the problem of producing material wealth that it will cease to be a problem at all, and men be left free to turn their attention to the satisfaction of other needs and desires?

It is not suggested that this point has yet been reached, or can be reached for a long time yet, over the world as a whole. Indeed, in many countries, poverty due to the under-development of productive power is still by far the

[1] Based on an article published in the *Encyclopaedia of the Social Sciences.*

most pressing problem. The masses in China and India are still desperately poor, not from unemployment or misdirection of productive energy, but from sheer inability to produce enough to provide for a reasonable standard of living. Their great problem is still to increase production in order to raise their own power to consume.

But in the great industrial countries of Europe and America the situation is rather different. Not that enough is being produced to give the citizens even of these countries a satisfactory standard of life. But in their case the further increase of actual production seems to be held back far less by a failure of productive power than by an inability to find means of distributing the increased real wealth which they are in a position to produce. Their problems are primarily unemployment, unremunerative prices, lack of proper balance between the output of different kinds of goods, dislocation of regular trading relationships between countries, and a creaking of the financial mechanism by which the exchange of goods has to be carried on. They could produce far more, with their existing resources, than they are producing at present; but they cannot do this because there is something seriously wrong with their methods of distributing and exchanging wealth. And there seems little chance that their powers of production will be allowed to develop as they could until these fatal defects in the structure of industrial Society have been somehow remedied. Meanwhile, production and the standard of life advance only by fits and starts; and progress is again and again interrupted by crises which cause the industrial nations deliberately to restrict their output of goods in an endeavour to create scarcity in place of a plenty which they have not yet learned to control.

How does such a situation arise? Obviously, the power to create more real wealth ought to be the means to a higher standard of living for the community as a whole. Obviously, on the whole and in the long run, it has been so hitherto—witness the great advance in the real incomes

of all classes in industrial countries during the past century. But it is no less obvious that this advance is less than it might be if the existing powers of production were being used to the full, and that, even so, it is made precarious by the liability of the economic system to recurrent crises and business depressions.

Industrialism is, fundamentally, an affair of productive technique. It is based upon the discovery and exploitation of improved methods of producing wealth, primarily in the processes of manufacture, but also to an increasing extent in agriculture and in the extractive industries yielding primary products. It is closely associated with an increase in the scale of production, with the development of capitalistic methods in both manufacture and marketing, and with the employment of wage-labour. Its secondary effects have included hitherto a concentration of the population in densely inhabited urban areas, a very rapid increase in the volume of international trade, much lending of capital for development by the more to the less advanced countries, and a very rapid increase in the number and social importance of the middle classes, including those engaged in the professions as well as in the administration and supervision of industry and commerce.

At the basis of industrialism is the machine. Both Capitalism and wage-employment are much older than industrialism, in the sense in which the term is used in this essay; and there were many factories before there was a factory system based on mechanical power. But industrialism can be said to have begun when machinery driven by a central supply of mechanical power became the typical method of manufacturing production. For from that point industry replaced commerce as the directing force of economic life, and the scale of production and the forms of business organisation came to be determined by the growth and character of mechanical power.

Thus, in England, where the Industrial Revolution proceeded a stage ahead of its development elsewhere, the industrial employer step by step ousted the merchant from

his previous predominance. The typical rich men of the seventeenth and early eighteenth centuries were not industrial employers, but merchants and financiers, engaged in buying and selling goods gathered together from a host of small-scale producers. There were some big employers even then; but they were not typical. The rich clothier whose memory is kept alive by his monuments and benefactions in countless English churches was not primarily an employer of labour, but a merchant, though the position of the small producers who supplied him may often have differed little in effect from that of wage-workers. The *bourgeois* class, to which the aristocrats of England and France before the great changes of the eighteenth century were compelled to pay some attention, was above all a class of merchants.

The Industrial Revolution, based upon a great series of mechanical inventions and above all else on the economic utilisation of steam-power, radically changed the situation. For it substituted for a relatively static system of production an essentially self-expanding technique. The merchant of the seventeenth or eighteenth century had indeed an incentive to expand his sales, as a means to additional profits. But there was for him, as a rule, no economy in buying on a larger scale, or in larger total amount; for the small producers who supplied him could not produce more cheaply merely because they were asked to produce more. It is a commonplace among economists that handicraft production tends to obey a law of 'constant cost', and indeed that, if additional workers have to be pressed rapidly into the service in order to meet an expansion of demand, costs will tend to increase on account both of the greater demand for labour and of the less skill of the new labour attracted into the trade. This was undoubtedly the position in handloom weaving in the eighteenth century, in that 'golden age' of the handloom weaver that preceded the introduction of the power-loom. The desire of the eighteenth-century merchant to purchase more goods from the small producers was therefore conditional on his ability

to sell more without reducing the price, or even while increasing it; and this, owing to the rapid expansion of trade with both America and the East, he was often able to do.

But as fast as machine-production based on mechanical power superseded handicraft, the situation was radically altered. Until then, the pace of production was set by the orders of the merchants, to whom the producers were for the most part merely subservient. But now the industrial employer, under the new factory system, had himself not only an incentive to get as large orders as he could, but also a means of stimulating the merchant's demand. For in most cases he could produce more cheaply by increasing his output; and he was therefore, unlike the handicraftsman, in a position to offer the merchant goods at low prices if only the merchant would increase his purchases.

This enabled the merchant in his turn to take new steps in stimulating demand, by offering goods at lower prices to the consumers, both at home and abroad; and the increased orders given by merchants under these conditions reacted upon industry. But the initiative in the system passed more and more into the hands of the industrial employers, whose offers of more goods at lower prices became the driving-force of material progress. From this point of view, the coming of industrialism meant in manufacturing industry the transition from a condition of constant to one of decreasing cost.

The industrial employer, who thus became the pivot of the new economic system, found himself urged on to new conquests by the pressure of the machine itself. He had to be abreast of his competitors in reducing prices; and this was a constant incentive to him both to increase his scale of production and to avail himself of the improved machines that were constantly being introduced. For, if he went on using obsolescent machines, there was no lack of rivals ready to supplant him; and, up to a certain point, his costs would fall as he was able to expand his scale of production.

There was, doubtless, even when the Industrial Revolution was at its height, an *optimum* size for any given business, beyond which it could not grow without loss of productive efficiency. But, as the *optimum* was growing larger with very great rapidity, the great majority of businesses were probably well below it, and racing to catch up. Accordingly, machine-technique gave the employer the greatest possible stimulus to increase his scale and quantity of production in order to cut his prices, and thus enabled the merchant to take full advantage of the elasticity of demand, especially in overseas markets.

I add this last qualification, because the strong competitive pressure on employers to reduce costs and prices, while it was a powerful stimulus to improved productive technique, reacted unfavourably upon the level of wages, and therefore upon the consuming power of the domestic market. The employer could cut his costs, not only by improving the efficiency of production, but also by reducing wages, or taking a firm stand against their increase; and this course appealed strongly to the less efficient employers, who were threatened otherwise with extinction. Relatively few employers could be brought to believe in Robert Owen's doctrine of the economy of good wages and conditions; and perhaps relatively few were efficient enough to make it true in their own case. The rapidly falling costs of the new industrialism were based on low wages as well as on a rapidly improving technique of production.

There was a second, and no less powerful, reason why wages and consuming power in the home market remained low in the period following the advent of industrialism. The new employers, under a constant necessity of improving their machinery and expanding their scale of production, were avid for fresh supplies of capital which they could apply to these purposes. But capital was hard to come by, in the days before the recognition of limited liability and the working out of the modern solution of joint stock companies and corporations based on widely diffused and easily transferable shares. The employer was therefore compelled,

as far as possible, to expand his business out of his own resources, living frugally himself and putting back his profits as capital for the increase of future profits. Living thus, and under this pressure, he was disposed to resent increased wages as sheer waste, diverting to useless expenditure resources badly needed for the expansion of output.

It is true that money thus saved was spent on buildings and machinery. But the constructional trades, powerfully stimulated as they were by the new conditions, did not quickly respond to the new technique, or pass over from handicraft conditions of constant cost to conditions of decreasing cost. Building remained, and remains in part even to-day, a handicraft industry, in which prices tend to rise rather than fall with any quick expansion of demand. And machine-making continued for a long time to be a highly skilled job, needing the services of skilled craftsmen who were in short supply, and to be incapable of being reorganised on a basis of mass production. Not until the methods of producing iron and steel, and of forging and casting, had been revolutionised in the latter half of the nineteenth century did the engineering trades become at all largely subject to the conditions of decreasing cost which had come to prevail in the cotton trade more than fifty years earlier. Consequently, spending on buildings and machinery did not expand production in the same degree as spending on consumers' goods, which were on the whole more easily mass-produced. This helps to explain the intense concentration of the new industrialism on the development of exports, and the constant search for new markets abroad.

Industrialism grew, then, at first above all in the textile trades, making Manchester the effective capital of the new industrial world. It was no accident that the economists who based their doctrines upon industrialism in this first phase came to be called the 'Manchester School', or that their outstanding dogma was a supreme faith in *laissez-faire*. For their own experience seemed plainly to demonstrate the self-expansive nature of the new industrial system, its capacity constantly to increase the supply of goods while

lowering their cost, and the value of competition in weeding out the inefficient producers and compelling the survivors always to adopt the latest advances in technique on penalty of being left behind in the race. What could be better than a self-acting system which at once benefited the consumer by lowering prices, rewarded the efficient with the high profits of the pioneer, and weeded out the inefficient who misused the resources of production? It was not clearly seen at this stage how far these results depended on the superior efficiency of Great Britain over other countries, of whose markets she was therefore able to take her pick, or how low wages must retard the growth of consuming power in the home market. These difficulties came later; and before they had been fully realised the character of industrialism had been greatly changed.

For, by and by, the new technique was extended from industry to industry, until it came to embrace the industries producing capital goods as well as consumers' goods. The development of railways played a dominant part in this transformation, not only because the railways enabled the interior of countries and continents to be opened up for economic development, but also because the demand for railway material gave an enormous stimulus to the metal trades and compelled them to devise and resort to mass-production methods. The new steel-making processes of Bessemer, Siemens, and Gilchrist and Thomas gave the metal-using industries for the first time a reliable and durable raw material to which methods of standardised production could be applied, and thus made possible the development of large-scale enterprise in the engineering and kindred trades, as well as the translation of shipbuilding from wood into metal. The same causes revolutionised the coal industry, greatly expanded already in the earlier phases of industrialism, and created a new and powerful grouping of 'heavy industries' to balance the older textile trades. With the coming of these new forces, the authority of Manchester began to wane; and industrialism, no longer so fully wedded to *laissez-faire* and competition, entered on a

new phase, which led on before long to the growth of trusts and combines, the recrudescence of tariffs, and in general to a renewed attempt at regulating just those processes of production and sale which the Manchester School held should be left severely alone by the State.

The explanation of this difference is not hard to find. In the first phase of industrialism, the maximum expansion of wealth could be secured by concentrating as far as possible on those forms of production which most clearly showed their obedience to a law of decreasing cost—in other words, primarily upon textiles. This could be done as long as there was adequate scope for the expansion of the sales of industrialised countries in markets where native producers were well behind in efficiency. But in time it became clear that this expansion could not continue unabated unless steps were taken to develop the complementary powers of production of these less industrialised countries, so as to increase the supply of goods which they could give in exchange for the mass-produced manufactures of industrialism. The railway was the great instrument of this development, opening up in the less industrialised countries vast new sources for the supply of raw materials and foodstuffs. Incidentally, this expansion helped greatly to raise wages in the industrialised countries, both because it enabled export to go forward at a greater pace, and because it secured an abundant supply of cheap foodstuffs. In the fourth quarter of the nineteenth century, there was a rise both in money wages and in the purchasing power of money, with the result that a great stimulus was given to consumption in the home markets of the industrialised countries.

In building railways and supplying railway material, and later in the supply of machinery produced on a large scale, the industrialised countries advanced to a new type of export trade vitally different from the old. The sale of cotton textiles or woollen goods was essentially a cash transaction, to be balanced at once by an equivalent purchase of goods. But the sale of railway material and other classes of capital goods could not be conducted on these

terms; for the purchase price could be paid by the buyers only if and when the railway or the factory became productive. Payment for such exports had to await the economic development of the countries to which they were sent, and then to be made in the products which their use had caused to be created. Consequently, this second phase of industrialism was marked by a great increase in the export of capital—that is, in the loan of capital in order to make possible the export of capital goods—from the industrialised to the less developed parts of the world. Great Britain especially exported huge masses of capital to all parts of the world, and above all to her own Dominions and India, to the United States, and to the South American Republics. She exported capital to Europe as well; but there it was as a rule more speedily repaid, as railways and factories built with British money were bought back by native investors.

It would take me far beyond the scope of this essay to describe the reactions of this growth of foreign investment on world politics and international rivalries, and on the development of Economic Imperialism. I am concerned here only with its effects on industrialism in a narrower sense. It made possible a very rapid growth of the industries producing capital goods, and speeded up in them the development of an intensified technique of mass-production. Whereas in the first half of the nineteenth century the typical instance of large-scale production was a cotton mill, by its close the types of large-scale enterprise were to be found above all in the heavy industries—in the great steel-making plants of Bethlehem or Middlesbrough, the great armament factories, the shipyards, and the great coal-mines already closely linked with steel. And, in the heavy industries, there was already a growing tendency for combination to replace competition, and for the size of the business unit far to transcend that of the single manufacturing plant.

But before we come back to the vital point hinted at in the last phrase, something must be said of the influence

of technical development upon business structure. As we have seen, the earlier industrialists were sorely hampered by shortage of capital. There was no investing public in the modern sense; and, broadly speaking, no one could invest money in industrial development unless he either lent it to a business man on his personal security, or became a partner in the business without the protection of limited liability, and therefore at the hazard of his entire fortune. The gradually extended recognition by law of joint stock organisation and limited liability remedied this difficulty, and opened the door to industrial investment by all who had savings or resources to spare.

Joint stock and limited liability not only increased immensely the total resources available for business expansion, but also removed the limits upon the size of capitalist concerns. Before their coming, the *entrepreneur's* difficulty lay in gathering together enough capital to equip and run a plant big enough to take full advantage of the economics of large-scale production. But now he was able not only to do this, but readily to expand the scale of business organisation so as to bring a number of separate plants under a unified control. The scale of business organisation was still being continually expanded by the inherent necessities of improving industrial technique; but it was now able, not only to reach these limits, but also to pass beyond them. Indeed, as the larger concerns were often at an advantage both in raising fresh resources in the capital market, and in getting credit from bankers and others, to some extent a premium was put on a scale of business organisation considerably larger than the technique of production in itself made necessary. In the early days of the trust movement there was a marked tendency for the increase in the size of the business unit to be dictated by financial rather than technological considerations; and this tendency was strongly manifested again in the troubled years after the war, in the gigantic mergers and concerns organised by Hugo Stinnes in Germany, and in the unwieldy

aggregations of businesses gathered under one control by Messrs. Vickers or the late Lord Leverhulme in Great Britain.

There was, however, side by side with these megalomaniac financial aggregations, a new technological tendency leading towards an expansion of the business unit on a scale very much larger than that even of the largest single plant. Under the earlier conditions of industrialism, the plant was the essential technical unit, and each plant could face its own technical problems independently of the rest. But the modern development of industrial technology is making the separate plants growingly interdependent in a variety of ways. In the first place, it is often essential, if the maximum economy in production is to be secured, to group together in very close relation and under unified control plants engaged in complementary industrial processes—in order, for example, to save intermediate transport costs on bulky half-finished goods, or to utilise a waste product, such as blast-furnace gas, in a subsequent manufacturing process. Secondly, it is often an advantage from the standpoint of economical production to reduce and simplify the varieties of a particular commodity placed on the market, and therefore to secure at least as much unity of control as is necessary to ensure this. And thirdly, the maximum economy is likely to be realised in many trades if each plant, instead of producing a wide variety of goods in competition with the rest, is in some degree specialised to the manufacture of a limited range of products, and thus enabled to produce, within this range, upon a larger scale.

The first of these technological requirements leads to a growth of vertical combination, that is, the linking up of successive stages of production under a common control. The second leads to fairly loose horizontal agreements between the firms at the same stage of manufacture, but need not disturb the independence of each distinct business. The third leads to much closer horizontal integration, as it is found in such businesses as Imperial Chemical

Industries, the English Steel Corporation, or the Steel Union in Germany.

Karl Marx, whose analysis of the industrialism of the first half of the nineteenth century remains the most penetrating study of capitalist development, has often been arraigned as a false prophet because he predicted a growing concentration of capital and an increasing polarisation of the two rival economic classes of capitalists and labourers. It is indeed the case that there is in modern industrialism no sign of the disappearance of the small employer, and that the growth of joint stock organisation has increased immensely the number of small part-proprietors of capitalist business. But, on the other hand, the small employer has become increasingly an agent, subcontractor, or hanger-on of large-scale business; and the great body of shareholders in modern industry have literally no say at all in its conduct or control. There has been a tremendous concentration, if not of the ownership, at any rate of the control of capital. The old personal nexus between employer and worker has been snapped; and the real struggle for power in industry to-day is to an ever-increasing extent between the few controllers of large-scale industry and finance and the organised force of the Labour movement, with the middle classes and the small investors as largely passive spectators of the conflict. Even the growing body of industrial technicians, who should, one would suppose, occupy a key position in the modern world, have been able but little to assert themselves as an independent force. They have been in the main merely the executive servants of large-scale Capitalism, though in many cases their personal sympathies might range them rather on the side of Labour.

We have seen how industrialism in its first phase concerned itself mainly with the sale of cheap consumers' goods in the markets of the less developed countries, and how, in its second phase, it supplemented this form of trade with the sale of capital goods, fostered by the lending of capital and credit overseas. The second of these processes,

like the first, cannot be expanded indefinitely without check. The first fails when it reaches the limits of the power of the less developed countries to offer more goods in exchange until their own productive resources have been more fully developed. This check leads on to the second phase; and this in turn fails when the burden of debts upon the less developed countries becomes so large as to check further loans. Moreover, as more and more countries pass under industrialism, their rivalry in selling goods and lending capital to the less developed areas fills up the available markets more swiftly. The advanced countries find growing difficulty in selling their goods and lending their capital overseas on favourable terms. They scramble for openings and concessions; and, as Marx foresaw, international rivalries are intensified, and crises of 'over-production' caused.

All this time, the technological revolution knows no pause. It is always impelling industrialists to produce on a larger and larger scale, and to create plants based on heavier and heavier capital expenditure. These can be operated at a profit, over and above the interest-charges involved in their construction, only if they are able to work full time, and to find buyers constantly for their full output. Post-war Germany, for example, when she 'rationalised' many of her industries with borrowed American capital, created a productive machine capable of producing very cheaply while it could be fully employed, but only at high unit cost if the volume of output had to be cut down through a failure of markets. The same conditions apply to many types of business in the United States and Great Britain, and indeed in every advanced industrial country.

It is therefore plain that the technical conditions of modern industry imperatively demand from the world of to-day an increase and a stabilisation of consuming power. In default of this, many of the greatest technical improvements are apt to mean not low costs but high, because of the heavy expense of the capital equipment on which

interest has to be paid. These high costs serve further to restrict demand, both because they result in high prices, often artificially maintained, and because they throw potential consumers out of employment, and so cut down their purchasing power.

But the increase of consuming power, up to the expanding limits of productive capacity, is a matter that industrialism, under present conditions, finds very hard to arrange. Herein lies the chief importance for the world of the gigantic experiment in Socialist industrialisation that is now proceeding in Soviet Russia. The Russians have set themselves not only to bring their industries up to the very last point of modern technological development—largely with the aid of American engineers—but also to industrialise in their vast country with its millions of peasant proprietors the technique of agricultural production. The socialised factories of Russia are of far less potential significance for the future of the world than her socialised farms.

But the importance of the Russian experiment does not lie mainly in the mere fact that the Russians are forcing on industrialisation at a hitherto unprecedented pace, but even more in the fact that they are doing this under conditions which ensure an outlet in consumption for everything that they are able to produce. With the entire control of production and distribution centralised, they are able to order what things shall be produced and in what relative quantities, and also to distribute enough purchasing power among consumers to ensure a sale for all the consumers' goods they can produce. All this, of course, can be done only within certain margins of error, and subject to their exporting enough goods to pay for what they need to import. But with the export trade in the hands of the State, they are not restricted to exports that can be sold at a money profit. Their foreign trade is, in essence, barter; and they can put on their imports prices calculated to represent the value of the exports needed to pay for them. Under these conditions, Russia appears to be immune from the fears of 'over-production' or 'under-consumption'

which beset the rest of the industrial world. To whatever other objections her economic system may be open, she seems to have solved the problem of balancing production and consumption, and thus to have set herself free to make the fullest use of every technical improvement in the arts of production.

This example of Russia raises a fundamental issue. How far are industrialism and Capitalism the same thing viewed from two different aspects? Or how far are they two different and separable things, connected only at a particular stage of the world's evolution? Historically, their connection is close; but they can by no means be identified. For, as we have seen, Capitalism existed long before industrialism, and took at first a mercantile, rather than an industrial, form. It is arguable that, as Capitalism preceded industrialism and was modified by its coming, so industrialism is destined to outlive Capitalism, taking on a new shape, as in Russia, under Socialist control.

For manifestly Socialism, the child of industrialism, will not speedily take up arms against its parent. Industrialism bred Socialism because it required the concentration of the workers into factories and their subjection to a common discipline of monotonous labour, and created in the factories an opposition between their demands for higher wages and the demand of the owners of the instruments of production for interest and profits. But Socialism cannot at present afford to be hostile to industrialism: for it bases itself on the demand for a higher standard of life for all, and therefore cannot dispense with the fullest possible use of every technical device which will serve to increase production and lighten the burden of labour. It is true that the workers to-day sometimes oppose the introduction of labour-saving devices, or other instruments of higher production, through fear of unemployment or out of hostility to the capitalist controllers of industry. But if, under a Socialist system, they get the instruments of production into their own hands, as they have done in Russia, they are bound to be on the side of changes designed to increase

output or to lighten labour. Possibly at a later stage of the world's history, when the problem of producing enough to afford to all a satisfactory standard of material living has been fully solved, the mass of the people may declare against industrialism, and express in deeds its preference for some other system; but assuredly that time is not yet. The advent of Socialism would intensify, and not retard, the progress of industrialisation.

This remains true despite the common indictment of industrialism that it condemns the great mass of the workers to a life of dull, monotonous, and even irksome toil. It is easy to contrast the skilled, varied, and interesting labour of the skilled handicraftsman with the deadening monotony of purely repetitive machine-minding. But, before industrialism, what proportion of the whole population consisted of skilled handicraftsmen? Was it ever as large as the number of persons, including those in supervisory and professional work, to whom the modern economic system affords interesting and diversified employment? If we contrast the modern machine-minder with the Gildsman of the Middle Ages, let us remember to contrast him with the medieval peasant as well. And, if we stress the effects of machinery in destroying craftsmanship, let us not forget what effects it has had—and the far greater effects it might have under proper control—in eliminating hard, disagreeable, unskilled, and brutalising labour.

The modern world cannot yet afford to restrict its use of machinery, both because there is much drudgery still to be eliminated, and because the growth of working-class power means an ever more insistent demand for a high and rising standard of life. If therefore Capitalism gives place to Socialism, the first phase of Socialism will be more intensely industrialist than Capitalism has ever been, because for the first time the whole community will be pulling together towards higher production over the whole field of industry and agriculture, and will also be seeking to save unnecessary labour in the management of domestic affairs, where the drudgery of housekeeping

is perhaps the most outrageous burden ever laid on half the human race.

It does not follow that industrialisation need in its later phases preserve certain of the features most prominently associated with it up to the present time. The process of urbanisation is still proceeding unchecked in the industrial countries; but its causes are now social quite as much as economic. The development of cheap road transport and of widely diffused electrical power is removing the technological reasons for dense urban concentration of industry, and preparing the way for a re-diffusion of it which will enable it to be carried on under far healthier conditions. But not much advantage is yet taken of these opportunities—though some is—because no less essential to the business than accessible power and cheap transport are an available supply of labour and housing and kindred accommodation for it. The business that wants to set up in the country has to attract its labour, and often to house it and help provide it with the amenities of life. It cannot readily take on fresh workers to meet a rush, or discharge workers when times are bad for fear of losing them altogether. Accordingly, as a rule only businesses catering for a stable demand are able to move out of the towns; and even such businesses are often deterred by the difficulties and initial capital costs.

Nor is this the only factor. Urban life has for the worker many attractions, in cheap amusements, varied society, the hurry and bustle of life, and a sense of nearness to the centre of things. It increases his freedom to change his job, and his independence of his employer, whose eye cannot be always on him out of working hours. Men and women leave the country for the town from preference as well as from necessity; and business tends to stay close by its sources of labour supply all the more because they are often the best markets as well.

But, here again, a Socialist system might make a great difference. For with the power of co-ordinated planning of industry in its hands, it would have also the power of

town and regional planning. It would be able, as the Russians are trying to do, to create new towns in the country areas, and to equip these with the means of a rounded and satisfying life, as only a few capitalists here and there have tried to do with Garden Villages and the like. Even so, a Socialist State would not succeed in decentralising and de-urbanising industry if the preference of the great mass of its citizens was for living close together in great towns. But at least the other obstacles in the way of decentralisation would be removed, as the technological obstacles are in process of being removed already, with the improvements in transport and the bulk transmission of electric power.

In suggesting that, under a Socialist system, industrialism would be intensified in order to provide a higher standard of life, I am not saying that there would not arise a keener demand for leisure. Indeed, I am sure there would. But the necessity of reconciling these two demands would only increase the pressure to make the most productive use of labour, to push rationalisation to the furthest possible point, and to eliminate all possible waste of human energy. Hours of labour would doubtless be reduced; but the tendency would be to put more labour into each hour, and then to aim at reducing the burden of this labour by increased mechanisation of processes. If mechanisation were applied with the conscious object of making labour less hard and irksome, as well as more productive, a great deal that is barely attempted as yet could be readily accomplished. The demands for more leisure and for more production do of course limit each other in some degree; but they are by no means incompatible.

Industrialism, then, does not connote Capitalism, although it is historically connected with it. The essence of industrialism lies in certain technical forms of productive activity which are capable of being directed to various economic ends and by radically different forms of economic organisation. It may be, as Marx insisted, that Capitalism has played an indispensable historic rôle in

the development of industrialism, because only under the control of the autocratic individual *entrepreneur* could the new technical forces have found free play. Certainly, it needed a strong directive energy to break up and replace the mercantile Capitalism of the pre-industrialist era, to destroy the domestic system of small-scale production and concentrate the workers in factories and towns, to accumulate capital at the expense of the immediate standard of living, and to force upon the State an attitude to industry consistent with the free growth of the new powers of production. Certainly the State itself, based on the aristocratic power of the landed classes, was at the time of the technical revolution quite unfitted to assume this directive rôle; and certainly the working class was equally unfitted, for it learnt cohesion and became a force only as a result of its experience of concentration and discipline under the new industrial system. Capitalism was, therefore, for the countries that led the way into industrialism, an indispensable stage; but it does not follow that industrialism, once created, depends on the survival of Capitalism for its effective operation.

Indeed, to use again a Marxian phrase, there are signs to-day that Capitalism has become a fetter upon the limbs of the industrial giant, holding back industrial development and checking the increase of production for fear of glutting the market. For the capitalist system of productive organisation is based essentially on the incentive of private profit. The capitalist *entrepreneur* will not, and cannot, go on producing goods unless he can make a profit by their sale. His market is therefore limited, not by the needs of the consumers, but by their willingness and ability to pay him a remunerative price. Because the prices he can get must tend to fall as the supply of goods in the market is increased, the *entrepreneur* is disposed to retaliate by restricting production in order to keep them up to a remunerative level. But this reacts on his costs, which tend to decrease with larger, and to increase with smaller, output. Everywhere in the world

to-day we can see frantic efforts being made to hold stocks of goods off the market, to buy up 'redundant' factories in order to close them down, to arrive at 'quota' agreements for the concerted restriction of output, and to maintain prices by 'valorisation' schemes at the cost of limiting demand. These are surely signs of something seriously amiss with the capitalist world.

Some say that all would be well if capitalists would but abandon their attempts to control the market, and go back to competition and *laissez-faire.* But there is no chance of their doing this, because so many of the factors of production that they have to use are now under control. The State limits their authority by legislation; and Trade Unions are too strong, both economically and politically, to allow wages to be governed by the mere higgling of the market under conditions of individual bargaining. Moreover, even if all these obstacles could be removed, where could world Capitalism hope to sell the vast mass of goods the industrial system is capable of producing, unless it were prepared to let wages rise to a point fully corresponding to the growth of productive capacity? And that would ruin the capitalists of any one country, unless either that country were isolated from the rest of the world, or all other leading countries did the same.

A return to *laissez-faire* is impossible. The concentration of capital needed for the full exploitation of modern productive resources is too great to be left uncontrolled by the State; for those who have this concentrated capital in their hands will assuredly control the State unless it controls them. But it is true enough that the attempts of capitalist combines to control production and prices are apt to defeat themselves, creating artificial scarcity, depression, and unemployment in place of the plenty which man's technical command over nature is making possible. Is not the truth that these partial controls, set up by groups of *entrepreneurs* for the maintenance of profits, will have to be gathered up into a wider unified control of industry, based on maximum production balanced by an equivalent emission of con-

suming power? There is nothing in this idea inconsistent with the development of industrialism. On the contrary, it seems that industrialism has now reached a stage at which its fuller development requires, above all else, coherent planning and unified control from the standpoint of consumption as well as of productive technique.

V

THE END OF THE BOURGEOISIE[1]

It is a strange fact that there has never been any word in English for *bourgeois*. A burgher means anything rather than a *bourgeois* in the modern sense. It makes an Englishman think of the Low Countries in the days of Van Artevelde, or of the burghers of Calais away back in the Middle Ages. The word *bourgeois*, while in default of a better word it has been used a great deal in English writing, has never become naturalised or lost its exotic flavour. It has retained to the end its italic quality. English writers have usually made shift with the words middle class—an awkward and yet a significant substitute for a more directly descriptive term. This is strange, because for more than two centuries England more than any other country, except perhaps Holland, has been the chosen home of the *bourgeoisie*. And yet it is significant too, for in England the *bourgeoisie* grew up within the structure of an aristocratic society based mainly on land-holding, and when it finally displaced the land-owning aristocracy in the control of public affairs, did this not by a direct conflict in which the aristocracy was overthrown, but rather by a gradual submerging of the land-owners in the rising tide of business prosperity. Perhaps this is why the *bourgeoisie* has remained in Great Britain even up to the present day consciously a *middle* class, lying in social status between an aristocracy largely bereft of political power but retaining much of its social prestige, and a working class out of which it has remained possible for individuals to rise into the middle class in considerable numbers even under the conditions of modern large-scale industrialism. The *bourgeois* epoch in Great Britain is not sharply marked off from the

[1] Originally published in the *Student World*, Fourth Quarter, 1932.

aristocratic epoch which preceded it, and maybe it will be no more sharply marked off from the Socialist epoch to which it is likely to give place. For throughout the age of Capitalism Great Britain has maintained a social structure which has combined a great deal of class differentiation and even more of snobbery with an absence of rigidity in its social castes. The British peerage and the British landed gentry of to-day are made up far more of *bourgeois* than of aristocratic elements, for creation and intermarriage have combined with investment and the entry of younger sons into trade to unify the land-owning and business classes into an economically homogeneous group. Social distinctions have remained, and the man in the street in England still 'loves a lord'; but there is commonly nothing except the fact that a man is a lord to mark him off from the plain commoner of equivalent wealth and income.

At the same time the boundaries between the middle and the working class have also worn thin. It is impossible in the Great Britain of to-day to say precisely where the middle class leaves off and the working class begins. It is impossible economically, for neither in standard of living nor in the way in which incomes are earned can a sharp line of division be drawn; and it is no less impossible socially, for there is no clear division of culture and mental outlook between large sections of the English middle class and the upper strata of the 'black-coated proletariat'. British society is not divided into a small number of clearly differentiated economic and social classes in such a way that every individual knows instinctively to which class he belongs. Class divisions go deep, but they are far more complicated than that. Indeed part of their strength in the Great Britain of to-day lies in the very fact that they are so ill-defined. For a very large number of people, uncertain of the class to which they really belong, have a snobbish preference for ranging themselves on the side of that which carries with it the superior social status. If class distinctions were more clearly cut, snobbery would lose much of its appeal.

It is therefore peculiarly difficult, under British conditions, to attach a clear meaning to the idea embodied in the title of this essay. It is difficult, for example, to say whether the ideal of the British Labour Movement is to end the *bourgeoisie* or to turn the entire population into *bourgeois*. Certainly the personal ideal of very large numbers of persons who are in the labour ranks is either to become *bourgeois* themselves, or to turn their children into *bourgeois* by giving them a better education, or at least one which will fit them to advance themselves in the social scale, and by getting them into a calling in life which ranks higher in social prestige. Yet in spite of all this fusion of classes and social ambitions, class differentiation is undoubtedly the very foundation on which society in Great Britain, as in the other countries of the Western World, is perilously based.

For the most part I shall speak in this essay of conditions in Great Britain, because I know them best, and shall leave the reader to interpret and adapt what I am saying in the light of his own knowledge of conditions in other countries. For there is immense variety from country to country in the forms of social stratification. Although modern Capitalism has created everywhere a powerful *bourgeois* class, this class is not everywhere the same in its inner structure, nor has it the same relations to other classes. The ending of the *bourgeoisie*, if it is to come, will not therefore be one and the same thing in all countries. For both the power of resistance of the *bourgeoisie* and the character of their influence on the new Society of to-morrow, will vary with the differences in the inner structure of the various *bourgeoisies* and their relationships to the remaining sections of the community.

Let us try at this point to define rather more closely what is meant by this term *bourgeoisie*, and by the suggestion that the *bourgeois* epoch in the history of Western Europe is drawing to an end. It is natural to think first of the use of the term which Marx and Engels made in the *Communist Manifesto* of 1848. The authors of the *Com-*

munist Manifesto drew a sharp distinction between two social classes both of which passed in their day for *bourgeois*. There was first the *bourgeoisie* proper, essentially the class which was growing rich and powerful by its success in the exploitation of labour with the aid of the new instruments of production and the expanding opportunities for trade. This *bourgeoisie* was pre-eminently an innovating class—a class which was rising to power with the development of the modern industrial system, and was intent to extract the last ounce of energy and power out of the new productive resources which were daily being made available for its use. This was the class which in one country after another, sometimes by revolution and sometimes, as in Great Britain, by constitutional reform, superseded the old aristocracy in the direction of public affairs and became the dominant influence both in the politics and in the way of living of the communities in which it was strong. But side by side with this rising *bourgeois* class, Marx and Engels pointed to the existence of the class of *petty bourgeois*—the very antithesis of the real *bourgeois* with whom they were often confused. For the *petite bourgeoisie*, as Marx and Engels used the term, consisted of those individuals and social groups who relied for their living and their economic status upon the survival of small-scale forms of production and trade. It included the small retail tradesmen, and with them the small masters carrying on business in workshops with little use of modern instruments of power production, and also the upper strata of the peasantry—*kulaks*, as we have learned from the Russians to call them in these days. This class, Marx and Engels said, would often side up to a point with the workers against the real *bourgeoisie*, because it felt its position to be threatened by the advance of large-scale industry and commerce. But at the critical point it was always liable to change sides; for it realised that the victory of the working class would inevitably sweep it and its social pretensions away and result even more than the advance of the real *bourgeoisie* in the supersession of small-scale methods in the economic system. It therefore pre-

ferred in the last resort to shelter in the nooks and crannies of large-scale industrialism rather than face total extinction as the result of the collectivisation of the economic processes of Society.

This definition of the *bourgeoisie*, with its two sharply contrasted sections, fitted on the whole well enough the circumstances and conditions of 1848. But it no longer fits the social stratification of the world of to-day. For there has arisen, side by side with the two sections of the *bourgeoisie* which Marx and Engels were able to identify, a new and powerful section which in their day had scarcely begun to assume a position of independent social importance. The typical employer of the first half of the nineteenth century was an individual, managing a business of his own, and financed partly out of his own resources and partly with borrowed money. Joint stock companies existed, but they were confined to a comparatively small part of the economic system. But in the modern world large-scale business has become increasingly impersonal. It has on the one hand its large body of shareholders drawn mainly from the upper and middle classes, but not for the most part closely or exclusively concerned with the fortunes of any one particular enterprise. The investor in these days spreads his money and his risks. It has, secondly, its large staff of employed persons, ranging from wage-earners who belong definitely to the working class, by infinite gradations through salaried employees of every sort and degree of responsibility and every gradation of income, to managing directors drawing incomes of many thousand pounds a year, partly as salaries and partly as profits and commissions or interest and dividends on private investments of their own. Moreover, side by side with this great and growing salaried middle class directly concerned with industry, there has developed another important and constantly swelling middle class of professional men—doctors, lawyers, consultants of a hundred different vocations—who draw their incomes either by way of salaries from public or semi-public bodies, or by way of fees either from business or

from the personal incomes of middle and upper class people. The richer a Society becomes, the more numerous this last section of its middle class grows; and together with the salaried employees of industry, commerce, and finance, it now represents more than any other group the characteristic by-product of the modern industrial system.

Now the difference between this new section of the middle class and those of which Marx and Engels were thinking is that its fortunes are not necessarily bound up with the continuance of private enterprise. Both the great and the petty *bourgeoisie* of the eighteenth and early nineteenth centuries were essentially individualists, who owed their position in society to their personal success in the exploitation of the business of production under their own control, and to their command of a body of labour, which they were able as individuals to employ at a profit. But the modern salaried *bourgeois* is not in this position. If he is engaged in industry or commerce, he is there as the employee of a large-scale business, which is usually a joint stock concern owned by a large number of shareholders, but may be a State enterprise such as the Post Office or a nationalised railway, or may lie on the border-line between public and private enterprise. If he is a doctor, he may be either in private practice or on the staff of a hospital or a municipality. If he is a teacher, he may be working in either a private or a publicly owned school or university. He knows, moreover, that even if the form of the ownership of the enterprise in which he is engaged changes, his services are likely still to be needed, and there will not be of necessity any change in either his remuneration or his social status. He is, therefore, not ranged inevitably on the side of private enterprise, nor is he necessarily an individualist in his social outlook. It is true that, as he has grown up in an environment dominated by private enterprise, and as most of those with whom he comes into close social contact depend for their living and social status on private enterprise, he has a strong tendency to take their side and to think of himself as at one with the *bourgeoisie* in the Marx-

Engels sense. But while this affects the social attitude of this new section of the *bourgeois* class, it does not dominate them to anything like the same extent, or with the same inevitability, as the older sections of the *bourgeoisie* are dominated by the conditions under which they get their living. The new *bourgeois* is far more open to conviction and far more ready if a struggle comes to take the stronger side.

While, however, the new *bourgeois* have to this extent an open mind, there are strong economic inducements to hold them to the side of Capitalism, as long as Capitalism appears to be a going concern with prospects of stable continuance. For while they have no ineradicable preference for private over public enterprise, they have naturally a very strong preference for larger over smaller incomes. They would not mind collectivism if collectivism could come in a *bourgeois* form, preserving in a new shape the class distinctions and differentiations of income which give them their status and their relatively high living conditions in the world of to-day. But they would mind very much being reduced to a condition of economic equality with the masses below them; and they would be unlikely to accept this position unless they were convinced that the forces coming up from below were irresistible. This kind of *bourgeois* is ready to change sides at the last moment, but hardly until he is quite convinced that the game is up.

In Great Britain to-day the disquietudes of Capitalism are causing the new *bourgeoisie* for the first time to develop a point of view of its own. Among it are found not only Fascists, demanding the forcible suppression of Socialism, but also the advocates of a 'planned national economy', of growing collectivisation without fundamental disturbance of the existing social structure, of social reform designed to fend off revolution and to give Society a new basis of stability without any *bouleversement* of ideals and ways of living after the Russian model. Those who think in this way—Mr. Keynes is an outstanding example — are disposed to minimise the differences be-

tween Capitalism and Socialism, or even to deny that either has a real and distinct existence of its own. They think of the problems of industry and finance primarily in mechanistic terms, as problems of increasing production and oiling the wheels of distribution through the introduction of new collective controls, trustification of industry, management of the currency, perhaps public control of new capital issues and of the direction of economic development. They do not recognise the existence of a class struggle or think in terms of any fundamental change in social values. They want the muddle and disorder of private enterprise to be cleared up, because they realise with Marx that the productive forces of modern industrialism have reached a stage at which they must be collectively controlled, unless the world is to be strangled by their unguided competition. But, this done, they cannot see why men should not live happy ever afterwards even in the midst of continuing economic inequalities; for they believe that if the world makes proper use of the modern powers of production, it is possible to end the extremes of poverty without making an attack on individual wealth.

Socialists, of course, envisage the problem of the modern world in totally different terms from these. For in their view class conflicts cannot be transcended by any improvement in the technical organisation of the productive system. They hold that competition and the struggle for markets are so much in the bones of Capitalism that there is no getting away from them without getting away from Capitalism itself. They hold, too, that Western Capitalism achieved the apparent stability which belonged to it in the nineteenth century, only because it was confined to a narrow range of countries, and found the rest of the world open to it as an expanding field for the marketing of its surplus products. They believe that within any capitalist country the large inequalities which at present exist necessarily involve a limitation of the market for goods below the technical capacity of the economic system to produce, with consequent under-production and

unemployment unless the surplus product can be dumped abroad. They do not believe that economic planning can be made real or can work successfully in an atmosphere of economic inequality; and above all, they believe that if the incentives of private enterprise, upon which Capitalism has predominantly relied in the past, are to be swept away or seriously weakened in their appeal, it will be indispensable to put in their place new incentives which will set men working as hard as there is need for them to work, in order to make the best of the productive resources at their collective command.

This question of motives or incentives is indeed fundamental. Every civilisation must have behind it a driving force—something that makes men feel it worth while to put out their energy in pursuit of an object which they make their own. In the capitalist world money-making has been the predominant object, erected into an ideal because success in making money has been regarded as the best proof of personal quality and as carrying with it the right to social status and consideration. It seems to me unquestionable that, if the economic system were collectivised without the introduction of equality, and if class distinctions were allowed to survive within the new collective system, the existing incentives to productive energy would be fatally weakened without any new incentives being brought into play in their stead. If this happened the *bourgeois* system would not end with any dramatic finale of revolution; but it would steadily and ineluctably run down, losing its momentum and its technically progressive character, and heading for a stagnation in which every creative impulse in life, art, and science as well as in industry would be bound to disappear.

Now the advocates of economic planning are undoubtedly right in their recognition that the world at its present stage of technical development has got past the point at which it can live successfully on the incentives of private enterprise. It is being collectivised willy-nilly, because the technical forces at its command are driving

it irresistibly to the introduction of a more and more extensive system of collective controls. In these circumstances the world's great need is to get a new set of incentives, which will fit in with the advancing technique of collectivisation. These new incentives must be collective rather than individual in their appeal. They cannot be based on the pursuit of individual wealth, or status determined by wealth or income. They must arise as the expression of a new collective impulse, to make the best for human happiness of the vast and growing productive resources which are at men's collective command. But they cannot take this necessary shape unless they are cut clean away from the idea of individual economic advancement, nor can they be so cut away as long as in the same community men are living side by side at standards of life so different as inevitably to divide them into social classes, with different cultures and antagonistic economic interests.

The strength of the new Russia lies of course in the fact that it is making the stimulation of these new collective incentives the very basis of its attempt to rebuild Society from the foundations. Russian planning is not primarily a technical affair, though it involves the use on a colossal scale of the most up-to-date technique of production. It is fundamentally far more an attempt to get men to live after a new way of life, and to respond to incentives widely different from those on which Western Europe still continues to place its half-hearted reliance. In one sense the Russians have an easier task than Western Europe can have in this new way of living. For the human material on which the directors of Soviet policy are endeavouring to play is predominantly raw material unshaped by Capitalism and almost a *tabula rasa* for the engraving of new social values. The task of Socialism in Western Europe is widely different from this; for *bourgeois* ideas and ways of living have bitten deeply into large sections of the European working class, and there is also in Western countries a far larger and more diversified middle class

then ever existed in Czarist Russia. That is why no simple imitation of the Russian experiment is likely to succeed in the countries of Western Europe. Communism, if it comes in Great Britain or in France or in Germany, will come in a form conditioned by the Capitalism out of which it will have to grow—conditioned by the strength of *bourgeois* culture and ways of living in large sections of the working-class population—conditioned, too, by the greater plasticity of the class structure in the more developed capitalist regions. But in this changed form appropriate to the conditions of Western Europe I am convinced that it will have to come; for the impulses which for two centuries and more have made the *bourgeoisie* a creative class, constantly increasing the sum-total of wealth and inevitably diffusing some part of that wealth over the whole population of the capitalist countries, have worn out, and I can see nothing save Socialism capable of taking their place. At least it will have to come, unless mankind in Western Europe is to sink into a Chinese stagnation; for I am certain of this, that no community of men can live successfully or even tolerably without the possession of a creative ideal. This ideal must be in harmony with the material conditions of their living. It must be such as to aid them in exploiting and developing the resources which are at their disposal. This being so, it must in the modern world be a collective and not an individualist ideal. That is why the *bourgeoisie* is doomed; for individualism made it a power and it is incapable as a class of conversion to a collective ideal.

VI

OUR UNUSED WEALTH[1]

It is a commonplace that the world of to-day, or at least that part of it which has reached a high stage of economic development, is suffering from needless poverty in the midst of plenty. An estimated total of thirty million workers unemployed, according to the International Labour Office, furnishes some indication of the extent to which the world is failing to use the resources at its command for the production of wealth. But estimates of potential production based merely on the numbers out of work are apt to sound unconvincing, especially to those who believe that crude human labour is being rapidly superseded as an agent of wealth-creation, and that the world is in a position to enjoy a far more generous allowance of leisure as well as a far higher aggregate of material wealth. Technocrats in America and Douglasites in Great Britain are not the only people who proclaim that it is well within our power both to consume more and to work less, and that unemployment quite fails to measure adequately the under-production which at present exists.

On the other side there are critics of a different sort, who maintain that the existence of a large mass of unemployed is no necessary indication of a corresponding power to increase production. This school stresses the world's fall from grace in respect of saving, and throws doubts on the adequacy of capital equipment to achieve anything like the promised increases in production at a reasonable cost. In face of these divergent views it is worth while to estimate, as far as we can, to what extent the world, or the leading countries in it, are at present failing to use not

[1] Based in part on an article originally published in the *New Statesman and Nation*.

simply available labour but combined resources of capital and labour available for the increase of production. This cannot be done at all completely or with any pretence to accuracy; but it is worth doing, even if the results are bound to be merely approximate and incomplete.

The first and most obvious evidence of a singular failure to make use of the available productive resources is furnished by the piling up of stocks of unsaleable goods, not in a few isolated cases, but of almost all the leading kinds of raw produce. In 1932 the world was carrying a stock of wheat more than twice as great as it used to carry before the slump set in. The stock of sugar had risen by about 150 per cent, that of tea by 50 per cent, and that of coffee by 100 per cent. Among raw materials, stocks of cotton had grown from 7½ million bales in January 1928 to over 10½ in January 1933, and of silk from 145,000 bales to 243,000. Rubber stocks had risen from 184,000 tons in July 1924 to about 634,000 at the end of 1932. Stocks of tin were up from about 25,000 tons in 1928 to 57,000. Lead stocks had grown from 48,000 to 177,000 since 1930, and stocks of zinc from about 40,000 tons in 1928 to 127,000 in Great Britain and the United States alone. Copper stocks were about 300,000 tons in 1928-1929, and about 700,000 tons early in 1933. These figures are of varying authenticity and completeness, and it is not possible to present them on a comparable basis for the different commodities; but there can be no doubt about their broad significance. For it can be safely assumed that the piling up of large stocks indicates a substantial reserve of unused current productive capacity.

A second and certainly not less valuable indication of the under-use of productive resources is furnished by the indices of actual industrial production now issued by a number of the leading countries. These, dealing chiefly with manufactures, serve as a complement to the figures given above for raw materials. It is worth while to set out the general figures for a few of the leading countries in tabular form.

GENERAL INDICES OF INDUSTRIAL PRODUCTION

	1928	1929	1930	1931	1932	1933 (2nd quarter)
United Kingdom .	100	106	98	89	88	91
United States .	100	107	87	73	58	71
Canada . .	100	108	92	77	63	62
Germany . .	100	100	90	74	61	68
France . .	100	109	110	98	76	86
Belgium . .	100	100	90	79	68	70
Czechoslovakia .	100	104	91	81	59	58
Poland . .	100	100	82	69	54	75
Japan . .	100	111	106	101	108	126
U.S.S.R. . .	100	124	156	189	207	213

These figures need a little elucidation. It will be seen that in the United States industrial production in 1932 had actually fallen to barely half the level of 1929—indeed it was during a substantial part of the year at less than half the 1929 level. In Poland also industrial production had fallen by almost a half, and in Germany, Czechoslovakia, and Canada by round about 40 per cent. In Belgium the fall was nearly a third and in France actually one-third. In Great Britain, on the other hand, it was only one-fifth, while Japan was not far below the level of industrial production reached in 1929, and the U.S.S.R. far above it, with a figure of industrial productivity which had more than doubled since 1928.

In general these figures clearly indicate a great unused reserve of productive capacity. There is clearly no physical obstacle to production to-day on a scale substantially higher than that which was reached in 1929, the last year before the coming of the slump. It is obvious that, if the increased supplies could be sold on profitable terms, every country could produce to-day a great deal more than it was producing before the slump began. This is clearest of all in the case of Great Britain, where large productive resources of both capital and labour were lying unused even in 1929. But it is true in a lesser degree of every country; for the

power to produce has been advancing faster during the past few years, while actual production has been declining, and no country, given an unlimited market, would find any difficulty in improving substantially upon the output actually achieved in 1929.

It is fair, in measuring the possible rate of advance, to take as an absolute minimum the rate of increased production actually achieved in the years before the slump. Between 1924 and 1929 world production of foodstuffs and raw materials was rising at the rate of about 3 per cent per annum. But in Europe the rate of advance, at any rate from 1926 onwards, was very much more rapid, averaging about 8 per cent over these three years. Industrial production, measured by the indices compiled by the various countries, was in most cases rising even faster than the output of foodstuffs and raw materials. Thus, to take only a few of the leading indices, Germany had increased industrial production by a quarter in the four years ending in 1929, France and Belgium by about 30 per cent in the last five years, Poland, Czechoslovakia, and Sweden by not far short of 40 per cent, and the United States by about 25 per cent. Over the same period in Great Britain industrial production as a whole had risen by only 12 per cent, but this low figure is accounted for partly by the severe depression in coal-mining, and if mining is excluded from the total the rise over the five years amounted to 16 per cent. Over the same period industrial production in the U.S.S.R. had gone up by over 300 per cent under the impulsion of the Five-Year Plan; but this is of course an abnormal instance. It is, however, noteworthy that Japan had increased her industrial output by about 44 per cent.

We need not, however, content ourselves with these general figures; for we can corroborate and amplify from other sources the evidence which they present. We can safely assume as a general proposition that the countries of the world would have no difficulty, if market conditions allowed, of producing again at least as much of any leading commodity as they have actually produced in any year

during the past decade. On this basis the fourteen leading coal-producing countries could easily turn out 50 per cent more coal than they were turning out in 1932. The eleven leading producers of pig-iron could increase output by 150 per cent, and the twelve leading producers of steel could increase output by over 140 per cent. The potential increases would be even greater if the U.S.S.R. and Japan were left out; but, on the other hand, they are smaller for Europe, excluding the U.S.S.R., than for the United States. Even so, Great Britain could, on this inadequate basis of calculation, double her output of both pig-iron and steel (actually she could do far more than this), and add at least a quarter to her output of coal. Germany could multiply her production of iron and steel by three, and add fully 50 per cent to her coal production.

It is harder, for lack of figures, to estimate the possible increase of production for most manufacturing industries. But something can be said of potential production in the textile trades and in engineering. In 1932 the output of the British textile industries, taken as a group, was about 17 per cent below the level reached in 1927, when actual production was of course already far below productive capacity. German textile production had fallen by 27 per cent from its peak point in 1927, and Belgian by 41 per cent since 1928. The French, Polish, and Czechoslovak industries were producing only about 60 per cent of their output of 1928. In the United States there had been a fall of 28 per cent in textile production from the level of 1929, despite the fact that production in some parts of the South had been relatively well maintained on a foundation of cheap labour, and despite a recovery from a still lower level of production during the latter part of 1932. It is safe to say that Europe could easily add a half to its present production of textiles, and would, if there were an adequate market, probably find little difficulty in doubling its output within a few years.

For engineering the figures are scantier. British production of engineering goods fell by about 27 per cent between

1929 and 1932, and French production by nearly 40 per cent; Belgian production fell meanwhile by more than a half, and German production by over 60 per cent. Shipbuilding suffered in all countries an even more sensational fall. Assuredly the world is in no danger of running short of the means of building more machines to make goods, or more vessels to transport them overseas, if only the problem of finding purchasers for the goods can be overcome.

It would be possible to prolong greatly this series of illustrative figures. The purpose of this essay, however, is not to exhaust the subject or the reader, but merely to give a general statistical indication that the common assertion of a vast potential increase in world production is fully capable of being verified. It can, of course, still be argued that the figures will not bear the interpretation placed upon them, because the world's productive capacity is lop-sided, and it is not equipped to produce more goods in the right proportions to enable them to be exchanged so as to meet an expansion of consumers' demand. But of what important classes of goods (except perhaps gold, which stands in a special position) is it alleged that a potential shortage exists? Certainly not of any of the leading foodstuffs or raw materials, or of any of the great staple manufactures. Nor, even if the world wishes to consume a higher proportion of its income in services rather than goods, is there any sign of a shortage of human beings capable of performing these services. Power-supplies are abundant, and can be rapidly expanded: there are abundant facilities for increased transport of goods; and there is plenty of building labour standing idle in every country.

It is nevertheless often asserted that any substantial rise in the total income in the hands of consumers would result in an increased demand for types of goods which the world economic system is not in a position to supply. To a certain extent this is undoubtedly true of particular countries, in the sense that a rise in the standard of living would lead to an increased demand for imports, which could not be paid for out of current international balances unless the demand

for these countries' exports rose in the necessary proportions. Great Britain, for example, would undoubtedly consume more foodstuffs if the standard of living rose, and whatever were done to increase British agricultural production, a certain part of the increased demand would be concentrated upon goods which cannot be produced on British soil. Especially would there be a largely increased demand for imported fruits such as oranges and bananas and apples. But we have had evidence recently in the early working of the Pig Marketing Scheme and of the Wheat Quota alike that the problem of increasing home supplies of many classes of foodstuffs is not nearly so difficult as it has been supposed to be. Indeed, the trouble with the stimuli recently applied to agriculture under the various marketing and similar schemes has been rather their tendency to produce an immediate increase far in excess of what was expected than the slowness of the agriculturists' response. Of course this has been achieved by throwing additional burdens upon the consumers by way of virtual subsidy to agricultural production. But in the case of those foodstuffs which Great Britain is at least as well equipped to produce as the countries from which she now draws her imports there does not appear to be any real reason, if only marketing can be efficiently organised, why the consumer should have to pay more even for a largely increased supply. The reactions of measures taken to increase domestic production of foodstuffs upon foreign countries such as Denmark have doubtless to be carefully considered; but these reactions will not occur in the dangerous forms in which they are occurring to-day if the increased home output is taken off the market by means of an increase in consumers' incomes rather than made a means of replacing imports from abroad. Surely it is evident that, if increased production can be brought about in this way, the greater prosperity will react to stimulate our export trade. For if we, by raising our standard of living, should make an increased call for imports from abroad, as it is admitted we should, is it not equally true that other countries, by

raising their standards of living, would make a larger demand upon our exporting industries?

Apart from foodstuffs, the effect of a rise in the consumers' standard of living would be found chiefly in industries in which there is no doubt at all of our ability greatly to increase domestic production, though of course this would be partly on a basis of increased imports of raw materials. It is interesting, for any attempt to estimate the probable effect of a rise in the standard of living in causing different degrees of expansion in different industries, to see what actually happened in the United States during the years when the standard of living was rising fairly sharply after the war. According to the figures quoted in *Recent Economic Tendencies in the United States*, the consumers' industries in which by far the largest expansion took place between 1919 and 1925 were, first, the automobile industry, and secondly the industries producing furniture and other house-plenishings. In spite of increasing mechanisation the American carpet industry increased the number of its employees by more than half, and the furniture industry by more than 30 per cent, as against an increase of only 20 per cent in the personnel of the automobile industry, where a rise of over 200 per cent in output was offset by a very high degree of mechanisation. Other industries which greatly increased both their production and their personnel include the canning, sugar, and ice industries, and the printing and allied trades. On the other hand the textile industries showed a much slower rate of increase in output, and practically no expansion in personnel, and most of the food-preparing industries showed a large decrease in the numbers employed, and no very large expansion in actual output. It is of course a well-known fact that a rise in the standard of living normally results in any relatively advanced country in a smaller proportion of total income being spent on foodstuffs, and a larger proportion not only on other consumption goods but above all on services.

This evidence from the United States cannot of course

be accepted as applying without substantial modification to European conditions, especially in the less developed countries. But for what it is worth it certainly does not seem to indicate that there would be any physical difficulty in meeting the demands for additional supplies of commodities which a rise in the standard of living would involve. The only industry in which serious difficulty might arise in securing a sufficient expansion of output to meet rising demand is the building industry, in which a limit is set to the possible rate of expansion over a short period by the potential shortage of skilled labour. Any attempt very greatly to expand housing all of a sudden would encounter serious difficulties over this problem, though of course in view of the present high level of unemployment in the building industry it would be possible largely to expand production before the point of labour shortage would be reached. Apart from this, however, Mr. Wheatley's success in 1924 in persuading the building industry to agree to a large augmentation of labour, and in actually increasing beyond what had been thought to be possible the output of houses during the next few years, shows that the difficulty of personnel could speedily be overcome if the building operatives were given a firm assurance that the increased rate of house-building was intended to continue over a period of years and not to be subject to sudden reversals of policy such as have occurred hitherto. For the builders are naturally reluctant to allow their labour to be 'diluted' by a large mass of newcomers as long as they are afraid of being confronted again within a few years by widespread unemployment. There should be no difficulty, if we once determined to embark upon a policy of increasing consumption up to the level of productive capacity, in giving the builders all the undertakings they can possibly desire. For apart from the still clamant demand for additional housing accommodation there stretches before us an endless programme of clearing away old poky insanitary houses as our standards of appropriate living conditions improve. What, then, are we waiting for save the

means of consuming the supplies of goods and services which can be readily placed at the disposal of the community as soon as the present deadlock in the commercial and financial system can be brought to an end?

But we are not here concerned with the reasons for the world's plight, or the best ways of escaping from it, but only to reinforce in a concrete fashion the generalisation that, if we are poor and getting poorer, it is by our own silly fault, and not because of any scarcity of the means of producing greater abundance. That some people, alive to this absurdity, have been led greatly to exaggerate the present potentialities of an increased standard of living is no reason for refusing to recognise that they exist, and that the failure to use them is a confession of the sheer failure of the capitalist civilisation of the twentieth century. In this essay these potentialities have been, not exaggerated, but deliberately and manifestly understated; even so they are great enough to give us all abundant cause for shame in the present, and for hope in a future when men shall have gained enough sense to make themselves masters of things, and to insist on bringing unnecessary and soul-destroying poverty to an end.

VII

THE PROBLEM OF CONSUMERS' CREDIT[1]

I

THERE has been during the past few years a good deal of discussion upon the question of consumers' credit, and many plans have been brought forward for the granting of credits directly to consumers in order to make an adequate demand for the growing supply of commodities and services which industry is in a position to produce. This advocacy of consumers' credit is natural enough in view of the circumstances of recent years, for even before the beginning of the world slump in 1929 there was ample evidence in many countries that the rapidly increasing powers of production at the disposal of mankind were not being adequately used, and that production was being damped down in order to maintain prices and avoid 'glutting the market'. It was widely suggested that this condition of things arose from some inherent tendency in the economic system as it is organised to-day for demand to lag behind supply, or rather for the supply of purchasing power to be progressively inadequate to purchase at the prevailing levels of prices the whole of the goods which Society is equipped to produce.

Those who hold this view have naturally been strengthened in their conviction by the coming of the slump and by the history of events since its beginning. For all over the world there has been, at least since 1929, an obvious deficiency of purchasing power in relation not only to the available capacity to produce goods and services, but also to the actual quantity of products seeking an outlet in

[1] Based in part on articles originally published in *The Christian Century* and in *The Millgate Monthly* in 1932.

the various markets. In these circumstances it is natural enough to suggest that this obvious deficiency of purchasing power can best be remedied not by the granting of additional credits to finance further production, but by the manufacture of a fresh supply of purchasing power to be credited directly to consumers in order to bring demand once more into equilibrium with supply at a remunerative price.

Views of this order, despite their evident plausibility, need to be carefully scrutinised, for there is often in the minds of those who advocate them some confusion of thought. The essence of the system of credit as it is now applied to production is that it is an advance of purchasing power, to be repaid as soon as the transaction which it finances has been brought to completion. The producer, when he gets a credit, is borrowing money which he will repay at a later stage when he has been able to sell his goods; and a merit commonly claimed for producers' credits of this type is that they are in essence 'self-liquidating', precisely because repayment becomes available as soon as the goods are sold. This, for example, is the case with trade bills under normal conditions; and the trade bill has served for centuries as a useful negotiable instrument precisely because it is held to possess this self-liquidating character.

It is true that under exceptional circumstances such as those of the present slump both the trade bill and the producers' credit granted by way of bank overdraft may lose their liquidity and become frozen, as has happened to the 'standstill' bills for which Germany and other European countries are in debt, and to many of the advances granted by British and American banks to industrial enterprises. It is indeed largely this loss of liquidity that has put the banking systems of the world into their present difficulties and caused them, in their search for liquid assets, to be less willing than before to grant fresh advances to countries or to industrial enterprises which are already 'frozen up' in consequence of the slump. But

these conditions are, or have been until lately, regarded as quite exceptional, and the provision of short-term credit as distinct from long-term capital for industry and trade still means in the minds of both financiers and economists primarily a granting of advances repayable within a limited and usually brief period of time on the completion of the particular transaction which they are designed to finance. In short, the essence of producers' credit as it now exists in the business world is that the advances of which it consists are repayable within a limited period of time.

Consumers' credit has already occupied an important place in the structure of modern business enterprise in at least two distinct though related fields. It has been applied on a large scale, particularly in the United States, to swell the purchases of the more durable types of consumers' goods through the institution of instalment purchase; and it has been used also on a large scale, particularly in Great Britain, for the purchase of house property with the aid of advances made by building societies. In both cases, as in the case of producers' credits granted by way of trade bills or bank overdrafts, the advances made are repayable; but these consumers' credits, especially those which are given for the purchase of house property, being destined for the buying of durable types of goods, involve repayments spread over a longer period than is normal in the case of credits granted to producers or traders for the financing of current business turnover. Accordingly, the consumers' credits involve a larger lock-up of capital resources and are of a less liquid type than the normal forms of producers' credit. Instalment purchase has been largely financed by means of the long-term capital resources of insurance societies and corporations, and housing credits have been provided largely by means of long-term funds invested in the building societies. This question of the degree of liquidity of the different types of credit is important, but it is not directly relevant to my immediate point, which is, that all the types of credit which have

existed hitherto have consisted of advances of purchasing power bearing interest and repayable at some future date. Indeed, the very word 'credit' seems to imply this condition of repayment; for it means that the creditor trusts the person to whom the credit is granted to make the repayment under the contractual conditions of the loan.

Some of the projects now current which pass under the name of proposals for the issue of consumers' credits differ fundamentally from any of the types of credit considered above, in that they are in effect proposals not for the advancing to consumers of an amount of purchasing power repayable at some future date, but rather for the direct manufacture of additional purchasing power, which is to be presented to the consumers without any condition of repayment in the future. Such schemes are not really schemes for the granting of credits to consumers, but for the sheer creation of an additional supply of purchasing power designed to remedy an alleged deficiency inherent in the working of the present business system. It is misleading to call them credits; for the use of the term introduces an intolerable confusion of thought, and serves to cover up the radical difference between repayable and non-repayable issues of purchasing power.

This rejection of the term 'credit', however, by no means disposes of the question, for the desirability of making non-repayable presents of purchasing power to the consumers depends on the truth of the contention that under the present economic system there does exist a tendency towards a permanent deficiency of purchasing power. This, then, is the question which has to be examined before we can hope to say whether such schemes as those of Major Douglas in Great Britain and Messrs. Foster and Catchings in the United States ought to be seriously considered. I have obviously no space in this essay to examine any particular scheme, and I must therefore confine myself to the general question whether the alleged deficiency of purchasing power can in fact be shown to exist.

In considering this question it is vital to begin by defining accurately wherein the supposed deficiency is supposed to consist.

(1) It is obvious to everybody that the amount of purchasing power available in the community at the present time is quite inadequate to purchase all the goods that the economic system is *equipped to produce*. In other words, it is obvious that *existing* purchasing power is at present far below *potential* productive capacity at the existing level of prices.

(2) It is obvious that the existing supply of purchasing power is quite inadequate to purchase all the goods which are at present on the market at prices remunerative to those responsible for their production. This is shown by the sharp fall in prices which has taken place in recent years, by the sharp reduction in dividends paid by industrial concerns, by the rapid fall in wage-rates, and by the precipitate decline of ordinary stock and share values.

(3) It is not, however, obvious that until the beginning of the slump in 1929 the total purchasing power available in the community was inadequate to buy the total supply of goods and services on the market, though even at this time the actual quantity of purchasing power was inadequate to buy all the goods and services which could have been produced if an adequate demand had been available at a remunerative price. For it is clear that, even if the total amount of purchasing power in the hands of the community were adequate to buy the entire supply of goods and services on the market at current prices, this would not necessarily ensure that the entire supply would actually be bought at the current prices, because some part of the available supply of purchasing power might be either withheld from current use or used to force up the prices of certain types of goods and services (*e.g.* capital goods), with the result of leaving a deficient supply of purchasing power available for the buying of other goods and services (*e.g.* consumers' goods) at the current prices, and thus either forcing down the prices of the latter types of goods and

services or leaving an unsold surplus to be accumulated in the form of stocks.

It was necessary to break up the general question of an alleged deficiency of purchasing power in this way in order to avoid confused thinking. Let us now consider for a moment how the available supply of purchasing power, with the relation of which to the current flow of goods and services we have just been dealing, is actually made up.

Under the existing economic system purchasing power comes into existence in one of two ways. It is either distributed as an incident of the process of production, or called into being by the issue of bank credits to traders or producers. The greater part of the current purchasing power of the community consists of sums paid out by productive concerns either as wages or salaries or as interest or dividends on capital or as rent for the use of land, buildings, and other durable instruments of production or as payment for materials purchased from other businesses at an earlier stage of production. The volume of purchasing power paid out as wages, salaries, and profits, and also the sums paid to other businesses for goods purchased from them for further manufacture or re-sale, depend directly on the prosperity of industry—that is to say, in part on the volume of production and in part on the prices at which goods can be sold. The sums paid out as rent and interest also depend finally on the prosperity of industry, but with a much longer time-lag in that they are contractual payments usually fixed in advance for a considerable period of time and therefore adjust themselves but slowly to the changing prosperity of industry.

It follows from this method of distributing purchasing power to the members of the community that anything which reduces either the volume of production or the prices at which the products are sold tends, other things being equal, to reduce the available quantity of purchasing power. Thus, if for any reason industry becomes less prosperous, the result is to diminish the amount of purchasing power which it is able to distribute, whereas any increase

in industrial prosperity connotes an increase in the total distribution of purchasing power accomplished by this means. The supply of purchasing power created by means of bank credits, which is the source of a large part of the purchasing power distributed by industry, also fluctuates directly with the prosperity of industry; for prosperous industrial conditions make bankers readier to lend and industrialists readier to borrow for industrial purposes. The total supply of purchasing power thus tends to move up and down with the prosperity of industry and with the output of goods and services, but not necessarily in the same proportions.

This is of course on the assumption that prices remain unchanged, whereas in fact they do not. Normally, as bankers expand credits the price-level tends to rise because the credits are issued in advance of the availability of the goods whose production they are used to finance. If, on the other hand, the supply of credit is kept stationary, an increase in the volume of production due to lower costs and improving efficiency is bound to react so as to cause prices to fall. Such a fall, however, need in these circumstances set up no disequilibrium, for *ex hypothesi* it is due to falling costs, and does not therefore decrease the *entrepreneur's* incentive to production.

There is in these conditions, apart from the possible complication introduced by a rise in prices due to the expansion of bank credit, to which we will come later on, so far no sign of any inherent tendency towards either a deficiency or a redundancy in the total supply of purchasing power in relation to the supply of goods and services. For the sums which are distributed as purchasing power together make up the prices which are charged for the goods and services offered for sale. The prices recovered by the sale of goods are simply the sum-total of the sums paid out as incomes (including corporate incomes and tax charges) in the course of production. This applies to the purchasing power created by means of bank credits fully as much as to any other kind, for bank credits are used as means of paying out

incomes (*e.g.* for wages and salaries) in advance of the sale of goods, and these advances are thereafter cancelled out of the prices realised by the sale of the goods in question. Interest on bank advances reappears in part as income of bank employees and in part as profit paid to the shareholders of the banks or applied as additional bank reserves. There is in all this no sign of an inherent tendency to disequilibrium between the amount of purchasing power distributed and the prices charged for the supply of goods placed on the market.

There is, however, always a possibility of temporary disequilibrium. If bankers expand or contract the total volume of their loans, the result is an immediate expansion or contraction in the total volume of purchasing power available before there can be time for a corresponding contraction or expansion in the supply of goods and services. An expansion of bank credit therefore tends to cause a redundancy of purchasing power at current prices, and so to lead to a rise in prices; while a contraction of bank credit (generally called deflation) tends to produce a deficiency of purchasing power at current prices, and to lead both to a fall in prices and to an increase in unemployment, and thus to bring about a further restriction of purchasing power.

Secondly, when industry is very prosperous—often to the accompaniment of an expansion of bank credit and of rising prices—the effect is so to alter the distribution of income in the community as to raise the incomes of the capitalist classes much more rapidly than those of the poorer classes. This results in an increased proportion of the available purchasing power being saved and invested, *i.e.* spent on capital goods, including existing securities as well as new capital goods, and a smaller proportion being spent on consumable goods and services. It is of course true than when more money is spent on new capital goods a large part of this additional money is speedily paid away in wages, directly or indirectly, and thus serves to raise the demand for consumable goods in advance of the appear-

ance as active agents of production of the new capital goods which the labour is being used to create. On this ground it has often been argued that the effect of an increased demand for capital goods will be a stimulus to the consumers' industries, and that it will accordingly serve to redress the balance and to provide a market for the increased output of the capital goods industries.

But this argument ignores an essential factor in the situation. It is quite true that the producers' credits flowing through the capital goods industries into the pockets of the wage-earners raise the demand for consumable goods, and thus tend to raise their prices, especially if the industries producing consumable goods are already in practically full employment. But in the first place this effect can be offset to the extent to which the new capital goods that are being produced result, when they come into action, in a displacement of labour. For under such circumstances the expansion in the supply of capital goods will only result for a brief period in an increased flow of consuming power; and as soon as the new instruments of production are actually installed the demand for labour will tend to fall off, and the total demand for consumable goods will be contracted by the consequent reduction in the wages bill.

It may well be that this is what actually happens in the course of business booms. The increased demand for capital goods results at first in an addition to the wages bill and therefore stimulates consumers' demand, but as soon as the new productive instruments get actually to work, so as to throw labour idle, the market for consumers' goods contracts, thus bringing the investment boom sharply to an end and causing a crisis of the familiar type. For despite the immediate effect of an increase in investment, which we have just noted, it remains true that investment in capital goods can continue to be remunerative only if the demand for consumers' goods continues to expand at a rate adequate to support the new investment. This may not happen, because of the relative depression of the share of the national income going to the poorer sections of the

community, especially under conditions of rapid mechanisation in industry; and the attempt to 'oversave', in this sense, may thus bring on a crisis due to a deficiency not in total purchasing power but in the amount of purchasing power actually expended on consumers' goods and services. The reverse conditions do not, however, appear in time of slump, because (*a*) the wages bill is then reduced not only by cutting wage-rates but also by discharging workers owing to slack trade as well as to the growth of mechanisation, and (*b*) because the form of purchasing power which is mainly in the hands of the richer classes is maintained by the stability and increase in the real value of fixed interest incomes.

It is therefore clear that (*a*) contraction of bank credit (*e.g.* deflation) can bring about a positive deficiency of purchasing power which may continue for a long time, until prices have been forced down to a very low level and production greatly contracted, when equilibrium may be at length re-established on a basis of low incomes, low production, and widespread and persistent unemployment. It is further true that (*b*) even without a deficiency of total purchasing power, there may exist in times of business prosperity a deficiency of demand for consumers' goods as opposed to investment goods, and this may be the cause of turning a boom into a slump, and bring about a positive deficiency of total purchasing power. It should be added that in time of slump there may also exist a deficiency of purchasing power applied to consumption goods, not because of over-investment but because of the unwillingness of the richer sections of the community to use their money at all, and of their preference for hoarding it in idle bank deposits.

These conditions are serious enough, but they are not of a character to be remedied by the granting of regular presents of purchasing power to the consumers, or by any manipulation of the purely financial part of the existing business system without other far-reaching changes in that system. For there is no evidence of a permanent or per-

sistent tendency towards a deficiency of total purchasing power in relation to the total volume of production. Accordingly, *save at exceptional times of deflation,* the creation of additional purchasing power in the form of non-repayable gifts to consumers would result in a redundance of total purchasing power in relation to the volume of products available for sale. This rules out of court any schemes which are based on the idea of a continuous creation of additional purchasing power by way of gifts to the consumers irrespective of the condition of industry from time to time.

II

We cannot, however, in view of the persistence of the idea that there exists under the present economic system a continuing deficiency of purchasing power in relation to current production, so shortly dismiss those who advocate as a remedy a direct subsidy to consumers' incomes. For we have still to deal with a second school of thought, which alleges not that the consumers' incomes ought to be increased but that the prices of goods should be lowered so as to enable the consumers to buy more without an addition to their money incomes. We must not, say the exponents of this doctrine, simply give people more money, for that would be inflation, such as occurred in Germany and other countries after the war. It would cause prices to rise in a cumulative fashion, and end by leaving us all worse off than ever. We must therefore try another way. Instead of putting more money into consumers' pockets, we must reduce—perhaps even halve—the selling prices of all the articles that they want to buy.

This, however, if costs of production remain unchanged, will evidently involve that numerous sellers of such goods will be making a loss by selling under cost price. Never mind, say our reformers of this school, we can make it up to the sellers in another way. Every trader who can produce proof of having sold goods at half their cost price (or what-whatever fraction may be fixed on as appropriate) shall

have the difference between his costs, including a reasonable profit, and his selling price, made up to him. This is to be done by issuing him a 'credit' through a new institution—let us call it the State Money Office. The trader will use the money which he gets in this way to pay the firms from which he bought his goods the full cost price of their production, including the producer's profit; and the producing firm will then use the money to pay off the bank overdraft which it incurred in order to finance the act of production. The bank, being thus repaid, will cancel the credit which it issued, and the whole process will have come to a happy end. The consumers' money will have bought twice as many goods as before; and yet the producer will have recovered the entire cost of production, including profit, and the banker will have been paid back the money which he lent. Assuredly, if it can be done, this is a charmingly simple way out of our present financial tangle.

But will it really work in this way? Let us agree that the banker, when he makes a loan to finance production, may be creating credits out of nothing. But these credits are thereupon used by the borrowers in meeting their costs of production. They are paid away to various persons —to workers as wages, to suppliers of materials, to transport agencies, to landlords, to insurance companies—in short, to a whole host of persons whose charges enter into the costs of producing the goods in question. The sums thus paid become in turn purchasing power in the hands of those who receive them, and in due course the recipients pay them away to other persons, who pay them away to yet other persons, and so *ad infinitum.*

As things are, the producer who has borrowed money from the bank in order to finance his production in due course sells his goods and uses the money which he gets for them—or as much of it as is needed—in repaying the credit granted to him by the bank. In this way a sum of money equal to that which the bank advanced is collected

from the public in payment for goods purchased and returned to the bank, which thereupon cancels the credit and so completes the transaction. The goods have been bought, the money has been cancelled, the cycle is complete. It is a case of 'as you were', except that the goods have been successfully produced and transferred to the consumer. There is neither more nor less money in existence when the transaction has been completed than there was before it began.

But now enter our reformers. The producer in future is not to recover from the public a sum sufficient to pay off his overdraft from the bank. He is to get—to take the fraction most commonly used for purposes of illustration—only half his cost back in the purchase price, and to derive the rest from the National Money Office, which is to create new money in order to reimburse him. This new money he is to use to pay off the bank (I am ignoring the intermediate stages, which do not affect the argument); and the bank will then be able to write off the overdraft and to regard the whole transaction as at an end.

So far, so good. But something seems to have been forgotten. For what has happened to the money which the bank originally advanced? It has been paid away, as we saw, to various persons who were active in various ways in the process of production, and they in turn have passed it on to yet other persons in payment for goods and services. The money advanced by the bank has gone circulating somewhere, and will continue to circulate from hand to hand as purchasing power until and unless some step is taken to recall it. But how, under the scheme which we are now considering, can it ever be recalled? Some of it—half of it, if selling price is to be half cost price—is recalled when the goods are sold, and to that extent the purchasing power originally created by the bank is cancelled when the bank overdraft is repaid. But what happens to the other half? It is not recalled in this way. It cannot be recalled at all under the scheme. It must continue to

circulate indefinitely as a lasting addition to the purchasing power in the hands of some person or other.

In other words, under this scheme every act of production will involve an addition to the volume of purchasing power. So far, so good. But this additional purchasing power, so far from disappearing when it has been used to buy goods in the first place, will last on indefinitely, to be used again and again in buying more and more goods for ever and ever. The total volume of purchasing power in the hands of the public will thus increase continually with each individual act of production. There will be more and more money, and every new commodity that is made will cause the creation of yet more money, to be used not merely for buying it, but again and again for buying one commodity after another.

How in these circumstances is it possible to contemplate, as the scheme does, the holding down of prices to the controlled level, or, if prices are held down, how will people possibly be able to spend before long a fraction of the money they will have? For at the reduced prices which the scheme postulates, there will soon be enough money in circulation to buy up all the available goods a dozen times over. Moreover, the longer the process continues, the more fantastically will the amount of money in people's pockets exceed the fixed prices of all the goods that there are available for them to buy. Everyone, as the saying goes, will have money to burn, for there will be no other possible use for it.

The fact is that this attractive project for enlarging everybody's purchasing power involves a simple fallacy. What its advocates say is that when the money from the National Money Office is used by the manufacturer to pay off his overdraft at the bank, the bank will cancel the credit issued to him and thus round off the transaction in a satisfactory way. But this is precisely what the bank cannot do. What it can cancel is not the credit issued to the producer, but only the producer's debt to it in respect of that credit. The credit itself has been paid away and has become pur-

chasing power circulating endlessly from hand to hand, and quite beyond the bank's power to cancel. It can be cancelled in only one way—by recovering it in the prices paid by the public for goods placed on the market. But this way is specifically barred by the school of reformers we are considering, since they insist that all goods must continue to be sold at less than cost.

As some people appreciate a concrete better than an abstract argument, let me illustrate what I mean. A boot shop sells a pair of boots which cost it at wholesale 8s., and needs 2s. more to cover its own costs. The reformers we are considering want to have the boots sold for less than 10s., and the seller credited with the deficiency out of the National Money Office. The seller is thus to receive 10s. and to pay away 10s. in costs and in his own living expenses. So far things seem to balance. But of the 10s. which the seller receives he gets only part from the buyer, say 7s. in order not to take too absurd a fraction; and he gets the remaining 3s. by way of newly created bank money. In this case, when he sells his goods, 7s. of purchasing power is retired, but only 7s. and not 10s., and the question is by what means the remaining 3s. is to be retired. For if it is not retired in some way, every fresh pair of boots that is sold under these conditions will cause the creation of an additional supply of money which can never possibly be retired by the sale of further goods because each fresh sale will engender *ad infinitum* an additional supply of money.

In these circumstances one of two things must happen. Either prices must rise when the supply of money increases, or, if this is prevented by fixed prices, consumers will be left with more and more money which they cannot exchange for goods because there will be no goods left to buy. The additional money will thus become absolutely useless, and the consumer will not in effect, as the scheme postulates, be selling at a remunerative price because a part of the money which he receives will be 'dud' money, devoid of purchasing power.

It may, however, still be considered that abnormal

conditions such as exist during a period of slump call for exceptional measures in the creation of consumers' purchasing power, for it may be urged that this would have the effect of raising prices and calling additional production into being, and that the proposed issue of additional purchasing power could be discontinued as fast as normal industrial activity was actually resumed. There is something in this, for certainly what is needed at the present time is a rise in prices leading to increased production and employment, and it is generally agreed that these results will have to be brought about by an increased issue of purchasing power. Why not, then, instead of attempting the difficult task of expanding bank credits in face of the reluctance of borrowers to incur additional obligations, make direct grants to consumers until purchasing power has been expanded to the requisite extent?

Why not indeed? But if this additional purchasing power is to be directly created, why not go one better and get something in return for it? In other words, why should not the State create the required additional money and use it to pay wages to the unemployed in return for useful work of a non-competitive and not directly remunerative kind? There are in any country any number of jobs of national reclamation and reconstruction that badly need doing but cannot be regarded as directly remunerative. Why, if additional money is to be created, should we not use this money to get these highly desirable works of social utility carried through? We have been told so often that they cannot be put through because the community cannot afford them. But the community can clearly far better afford to pay out money for something than money for nothing. The only necessary condition is that the works shall not be of a competitive or directly remunerative kind.

Let us, however, realise that, if this is to be done, it will be a measure of a quite different order from the granting of additional bank credits on the traditional lines. For the essence of the success of the proposed addition to the volume of purchasing power is that the sums paid out to the con-

sumers shall not be repayable at any future date. They will take the form of a permanent addition to the community's supply of money, at any rate until and unless the community itself decides to redeem them and so again contract the supply of money. Unless this is done, the new money will continue to circulate indefinitely; for it is not true, as some credit reformers seem to suppose, that when a sum of money has once been spent that is an end of it. Spending money does not cancel it, but only transfers it to a new owner who can then spend it all over again—and so *ad infinitum*. Consumers' 'credit', so called, can therefore be effective for the purpose in view only on condition that it is not credit at all, but a fresh creation of money destined to remain permanently in being. This is nothing against the project; for if the community raises both the level of prices and the volume of production—and these are the ends which the scheme is designed to serve—a permanent addition to the supply of money will be needed in order to finance the increased volume of monetary transactions. Let us not be frightened of the proposal merely on the ground that it involves a permanent addition to the supply of money, for if we want to raise both prices and production a permanent addition to the supply of money is precisely what is needed. But let us at any rate go into the scheme with our eyes open, realising that it is not a plan for the emission of a new type of credit, but definitely a plan of monetary 'reflation' designed to bring about a permanent increase in the supply of money without at the same time adding a new burden of debt, and interest upon debt, corresponding to this increased supply. I think that as soon as the real character of the project is clearly understood it will become obvious that it is far better to use the new money to be created under it for financing desirable jobs of social utility than in making mere grants to consumers without getting any service from them in return.

But perhaps we have not yet done with the schools of credit reformers who put their faith in monetary expansion to be achieved by the granting of additional

credits; for these projects take a new shape every time one of them is successfully exposed by criticism. Accordingly I must now go on to discuss in rather a more fundamental way the underlying fallacy involved in most achemes of this kind. On the assumption (with which I shall deal later on) that there is no time-lag at all between production and consumption, the selling prices of goods reappear completely in the incomes of those who contribute to their production. Thus, if a = the incomes distributed as wages, salaries, rent, interest, and profits by the retailers, b the similar incomes distributed by the wholesalers, c the similar incomes distributed by the manufacturers, and d the similar incomes distributed by the bankers who advanced the credits necessary for production, then $a + b + c + d$ = the selling price of the goods. This equation is not affected by the price at which the goods are sold; it exists at any price level. For high prices will increase the total distributed as wages, salaries, rent, interest, and profits in like proportion. Of course, incomes distributed include collective incomes, such as profits placed to reserve or deductions from wages for contributory pension funds, and so on; for these incomes are also spending power. If, then, a deficiency of purchasing power *actually expended* arises, it can arise only from the withholding of some of the available purchasing power from actual spending, and not from a deficiency in the amount of available purchasing power. That is, on the assumption made at the opening of this paragraph.

But obviously there is, in fact, a time-lag, and this causes the possibility of a further deficiency, or of an excess, in purchasing power. For (a) if some purchasing power is withheld, as above, it will react to force down the prices of the goods appearing on the market at the time when this occurs (*i.e.* of goods produced at an earlier period). This will react to decrease both current production and the current distribution of purchasing power, so as either to reestablish equilibrium at a lower level or, if the withholding of purchasing power from use continues (as it well may do),

to create a new deficiency of spending even at the lower level, thus accentuating slump conditions.

Moreover (*b*) increases or diminutions in the volume of bank credit, unless they keep pace, as they seldom do, with the fluctuations in the supply of goods on the market, will result in a current excess or deficiency of available purchasing power at the prevailing prices. They will thus force prices up or down; but the readjustment of spendable incomes consequent on the change in prices will only come into play gradually over a period of time. Bank credit, having these properties, could be used to correct the disequilibrium arising from the withholding of purchasing power under (*a*); but in fact it may operate as an exaggerating factor, because the withholding of purchasing power usually arises from under-investment or currency hoarding in times of depression, and at such times the banks will tend to restrict credit for lack of borrowers whom they regard as sufficiently solvent.

There exist, then, serious tendencies in the economic system to a lack of balance between the total prices charged by business and the incomes which buyers are prepared to spend, and such disequilibrium is at the least a powerful cause of the deepening and prolongation of business depressions. But there is in this no warrant for the view that matters could be put right by reducing the prices of goods and at the same time recouping their sellers by a creation of fresh money. For, if this were done, the reduction in prices would be likely to call the withheld income into play, and this income would appear in the market side by side with the new money created in order to recoup the sellers for the reduction in the prices of their goods. This would create a redundancy of purchasing power, which would either cause prices to rise or, if this were prevented by law, leave consumers with an unspendable surplus of money in their hands.

Moreover, as we saw, this creation of new money would be cumulative; for every fresh sale of goods would involve a fresh issue of money without an equivalent cancellation.

In respect of each process of production and sale there would be (*a*) an initial issue of bank credit to the producer, which would then be paid away in incomes to those concerned with the production, and (*b*) a final issue of credit to the consumer, which with the price paid for the product would go to repay, and so cancel, this initial credit in the books of the bank. But this act of cancellation would not cancel the incomes paid to those concerned with production on the strength of the initial credit, but only the initial credit itself. The incomes in question would be cancelled only to the extent that they were expended on buying goods, and up to the limit of the prices charged for the goods. Thus, if half the seller's costs (including his profit) only were covered by the price, and the other half by a fresh creation of money, only half the incomes paid away to those concerned in the production could be cancelled by the purchase of the product, leaving the remaining half to be expended—on what? On nothing; for there would be no goods left for sale. This unexpended money would therefore remain in being, receiving a fresh increment with each fresh passage of a new product to the stage of sale to the consumer. What I have called the unspendable surplus would be cumulative; and the supply of purchasing power would soon become astronomical, without being allowed to act, as in ordinary inflation, on the level of prices. Of course the proportion of one-half is only meant, by those who use it, to be illustrative; but whatever the fraction, the same dilemma arises, if there is to be any reduction at all of prices below costs.

What, then, is the element of good sense in this unworkable project? That the economic system can only work well and smoothly as long as the spending power available *and actually used* keeps pace with the volume of productive capacity, so as to enable all that can be produced to be sold at a price to cover costs, provided only that the different commodities and services are produced in the right relative quantities. The moral is that we need (*a*) a collectively planned economy designed to secure the

right relative application of productive resources to the various kinds of production, (*b*) a mechanism of income distribution which will base the amount of income which it distributes on the magnitude of the available productive resources, (*c*) a system of controlled prices to preserve the proportion between the planned production and the amount of income distributed, (*d*) a controlled financial mechanism designed to correct disequilibria due to the time factor, or to any tendency to leave available income unspent. In other words, a complete Socialist system. The idea that the required equilibrium on a basis of maximum production can be secured under Capitalism by manipulating the mechanisms of price and credit is a myth and a delusion.

VIII

DR. HAYEK'S TRIANGLE[1]

DR. HAYEK'S 'triangle'[2] has been invoked a good deal during the past few years by monetary writers, who have based upon it certain conclusions concerning the inevitable effects of inflation on the productive system. Before we attempt to consider these conclusions, it seems appropriate to get quite clear about the nature of the 'triangle' itself, and the economic situation which it is designed to illustrate.

Of the triangle's three sides, as they appear in Dr. Hayek's Fig. 1, the base represents the money value of the supply of consumers' goods that is being marketed at a particular time. At least, I think this is what it is meant to represent. The vertical side forming a right angle with the base bears two labels. It is labelled 'intermediate products'; and it is also, by means of an arrow, labelled 'time'. It appears to represent, as a line, the period of time which it takes for a typical unit of 'original means of production' to be converted into a unit of 'consumers' goods', whereas the lines that branch off from it at right angles, to meet the third side of the triangle, appear to represent the money values of the intermediate products existing at each stage of the process of production. The third side of the triangle, slanting across to connect the other two, appears to indicate the successive doses of 'original means of production' used up in producing the final supply of consumers' goods.

The remaining significant feature is the area of the triangle. This, Dr. Hayek tells us, 'shows the totality of the successive stages through which the several units of original

[1] Based partly on a paper read to 'Some Oxford Economists' in February 1934.

[2] I know, of course, that Dr. Hayek did not invent the triangle, which is much older; but I am dealing in this essay with the use which he makes of it in his *Prices and Production*.

means of production pass before they become ripe for consumption'. And 'it also shows the total amount of intermediate products which must exist at any moment of time in order to secure a continuous output of consumers' goods'.

If I understand Dr. Hayek aright, his 'triangle' represents directly not goods but money; for he insists on this point, though he speaks at times as if it represented the flow of goods. I shall, however, assume that what is directly represented is the money goods are sold for, and not the goods themselves. The triangle as a whole therefore shows either (*a*) the money-value of all the goods, final or intermediate, that are being sold at a particular time, or (*b*) the total money-payments involved in all the sales necessary to put a given supply of final goods into the consumers' hands.

Let us now take the three sides of the triangle one by one. The base, as we have seen, is labelled 'output of consumers' goods'. Consumers' goods are here distinguished from producers' goods, which appear elsewhere in the triangle. As the whole figure represents money-values rather than the goods themselves, we can take the base to stand for the total money-income spent on consumers' as opposed to producers' goods at a particular time, *i.e.* total 'spending' as distinct from 'saving' or 'investment'.

Let us next take, not the vertical line marked 'intermediate products', but the connecting line. This represents, on a simplified assumption the nature of which Dr. Hayek makes plain, the successive doses of 'original means of production' applied in the successive stages of manufacture of the final product. The assumption is that the means of production are applied in continuously uniform doses throughout the process of manufacture. This assumption is not necessary to Dr. Hayek's argument; but it usefully simplifies the presentation of it.

The 'original means of production' here referred to are, Dr. Hayek explicitly informs us, 'land and labour'. They do not include capital. In fact, what is represented is presumably not the 'land and labour' as such, but their money

value, *i.e.* the successive payments made for the use of the land and labour applied at each stage of production. Here, as elsewhere, Dr. Hayek makes the common assumption that the money-values, or prices, stand for the real things they are the means of exchanging.

The vertical side of the triangle stands for two different things, because the triangle itself is being regarded in two different ways. It can be a picture either of the entire productive system as it exists at a particular moment, or of the complete history of a particular productive process over the entire time occupied in the passage of goods from a raw to a finished stage. In the first case the vertical line, in conjunction with the slanting line, serves to measure the value of all the intermediate goods in existence at all stages at a particular time. Or rather, this is indicated by the sum of all the dotted lines which cross the triangle parallel to the base. In the second case, the vertical line stands directly for the period of time occupied by all the successive stages of production taken together.

Dr. Hayek's first important use of his triangle, beyond the emphasising of certain obvious truths, is made in connection with the influence of changing methods of production upon its shape. He argues that as production becomes more 'capitalistic', that is, as more capital is applied, in conjunction with the 'original means of production', in the making of goods, the process of production as a whole becomes 'longer' and more 'roundabout'. This involves, he says, a lengthening and narrowing of the triangle, as the greater lock-up of money in intermediate goods, which is in his view the same thing as the increased application of capital to the productive process, leaves a smaller supply of money available for purchasing the final products which issue out of production in the form of consumers' goods. Dr. Hayek is of course assuming at this stage that the total supply of money available for all purchases, both of consumers' goods and of intermediate goods and original means of production, remains unchanged.

At this point my first serious difficulty arises. I agree,

of course, that if out of a fixed supply of money more is applied to purchasing other things than consumers' goods, less must be left for the purchase of consumers' goods. That is evident. I also agree that an increased rate of investment must mean, under these conditions, a decreased supply of consumers' purchasing power expressed in money. But I do not agree that a more capitalistic method of production by any means necessarily lengthens the *time* which the entire productive process takes. It may indeed shorten it, as it does when the fresh capital is applied to improving the methods of transport, or to grouping together, for speedier execution in a single works, successive processes previously carried out in separate establishments, so as to eliminate time and transport involved in less capitalistic methods.

If, therefore, Dr. Hayek's vertical line represents 'time', as he says it does, I cannot agree that the use of more capitalistic methods of production will necessarily involve any lengthening of it. It may even become shorter instead of longer, and is, I think, tending to do this under modern conditions of capitalist organisation. This is important; for obviously an increase in the number of stages at which unfinished commodities are exchanged will tend to speed up the velocity of monetary circulation, if it is accompanied by anything less than a proportionate increase in the total duration of all the stages of production taken together. It can, however, be argued that, although Dr. Hayek says that his vertical line represents time, this is not really what he means, and that he really intends it to represent the number of stages involved in the process of production as a whole, irrespective of their duration. If this is what Dr. Hayek means, as it often seems to be when he is referring to more 'roundabout' methods of production, it is a pity he ever introduced the conception of 'time'; for emphatically 'longer' and 'more roundabout' do not mean the same thing, as he seems to assume that they do.

But, even so, I am unable to accept Dr. Hayek's view

that more capitalistic methods of production, *i.e.* those involving a larger application of capital, are necessarily more 'roundabout'. Often, on the contrary, a more capitalistic mode of production may mean the elimination rather than the insertion of a stage. I do not suggest that it does necessarily mean either; for most often the number of stages is not changed by the application of more capitalistic methods. But where it is changed, there may be either an increase or a decrease: there need not be an increase as production assumes more capitalistic forms.

I realise that Dr. Hayek bases his argument on a situation from which he has eliminated the effects of technical change. But I am wholly unable to attach any realistic meaning to this process of abstraction. What is 'technical change'? Is it (*a*) simply new inventions, or (*b*) any change in the technical structure of industry, including changes due both to new inventions and to the increased application of inventions already made? I think Dr. Hayek must mean (*a*); but I can see no difference in the effect produced by the one type of technical change as against the other on the structure of industry. If Dr. Hayek means (*b*), I am quite unable to conceive of the industrial system becoming more capitalistic in any way which does not essentially involve and include technical change.

But perhaps Dr. Hayek will argue that I am mistaking the nature of his 'stages' of production, and that they represent, not technical stages, but money stages, *i.e.* stages at which intermediate products are exchanged against money. This is indeed the assumption on which Dr. Hayek appears to work in the earlier part of his argument; but he explicitly discards it later on, when he recognises that more capitalistic methods may be accompanied by an integration of businesses that actually lessens the number of times the intermediate products change hands. It therefore certainly cannot be assumed that more 'roundabout' production involves a productive process divided into an increasing number of *money* stages. Yet Dr. Hayek does appear to base his main argument on this assumption,

though he attempts to make allowance for its falsity *after* reaching his general conclusions with its aid.

It can, however, still be argued that the conception of more 'stages' of production, though Dr. Hayek appears to lay great stress on it, is not really vital to his argument, and that his real point lies simply in the increased lock-up of capital in intermediate products which more capitalistic production involves. In one sense this is a mere truism; for if a larger proportion of a fixed money supply is being used as capital, that evidently means that more capital is being locked up. The two statements signify exactly the same thing. The question, however, is whether a resort to more capitalistic methods of production does mean that a larger proportion of total income must be locked up in intermediate products. Plainly it does not; for if total productivity is increasing uniformly over all industry, a given amount of money will buy more intermediate as well as more consumers' goods: so that production can become more capitalistic without any shift in the proportion of money spent on the two kinds of goods. But it may still be true that an increased proportion of saving out of income must have the effect of accentuating the capitalistic character of industry; for where else is the increased saving to be absorbed?

Dr. Hayek argues that, if the receivers of income do actually spend less and invest more, a larger proportion of total money-income must be locked up in intermediate goods, and this must cause production to become more capitalistic and roundabout than it would otherwise be. More capitalistic, yes, provided that the money saved is actually invested, and provided further that it is invested within the economic system in question. But not of necessity more 'roundabout'; for the two are not the same thing. Dr. Hayek's triangle may become narrower at the base without becoming any taller in respect of either time or number of stages, with the consequence that, on his assumption of a fixed money-supply, it will have to bulge. The sloping side will cease to be a straight line, and become

a curve. This will happen if more capital is locked up at each stage of production, without an increase in either the time taken or the number of stages. It can be argued that, if this happens, Dr. Hayek's essential point will hold good all the same.

What is his essential point? He begins by assuming that the original shape of his triangle represents a condition of equilibrium, in which all the factors of production are fully employed. He then goes on to point out, quite correctly, that any change in the balance of spending and investment is bound to alter the shape of the triangle, and so to disturb the existing equilibrium. But he seems to hold that, provided that the total amount of money remains unaltered, equilibrium can be established at any relative distribution of this supply of money between spending and investment, the only difference being that different distributions will carry with them different degrees of 'roundaboutness' in the productive processes. Furthermore, he holds that, whereas a change in the balance of spending and investment brought about by an increased emission of money is bound to be unstable and impermanent, a change brought about by increased or decreased investment out of a fixed supply of money can be relied on to be permanent, and therefore to serve as the basis of a new equilibrium. Let us look at these opinions in the light of the 'triangle'.

First, is *any* relation between spending and investment consistent with equilibrium? In order to answer this question, we have to begin by assuming that a relation consistent with equilibrium has existed, and that a change in this relation has then occurred, without any change in the total supply of money. What conditions have to be satisfied in order that a new equilibrium may become established? Let us assume that the change is one that increases money investment at the expense of money spent on consumption. In that case, the reduced sum of money now available for the purchase of consumers' goods has to buy, not merely as many goods as the larger amount of money

previously bought, but also the additional goods which the increased application of capital now permits to be produced. For presumably the increased sum spent on intermediate goods does result in an increased flow of consumers' goods, so as to make the process of production more capitalistic still. But this would only increase still further the ability of the economic system to produce consumers' goods; and unless the rate of investment went on increasing more and more *ad infinitum*, an increased supply of consumers' goods would have some time to be marketed. For clearly the only use of intermediate goods is to issue, sooner or later, in consumers' goods.

Accordingly, the prices of consumers' goods must fall more than in proportion to the reduction in the income available for their purchase. In other words, an increase in investment is reconcilable with equilibrium only if it enables such reductions to be made in the prices of consumers' goods as will enable a reduced consumers' income to buy more goods than before up to the point necessary to carry off the increased supply. Unless this condition is satisfied, an increased rate of investment, resulting in an increased lock-up of capital in industry, will not be consistent with the establishment of a new equilibrium.

Dr. Hayek appears to assume that the required fall in the price of consumers' goods will necessarily be brought about in part by means of a fall in the rate of interest. For the demand price for capital depends in the last resort on the demand price for consumers' goods at the margin, and if this latter price falls it is bound, unless the relative distribution of income between the owners of capital and the 'original means of production' is altered, to bring down the demand price for capital to an equivalent extent. This tendency to a falling rate of interest will therefore check accumulation of capital, until equilibrium is restored. The point at which it will be restored will depend on the response made by savers to a fall in interest rates, in other words, on the elasticity of the supply of new capital. Thus, equilibrium can in theory be restored at any ratio between saving

and spending, if there is no limit to the lowest rate at which savers are prepared to invest. But, so far, this restoration of equilibrium may apparently demand a derisory rate on new capital, or even a negative rate; and the new ratio between saving and spending, even if it is established by means of an increase in voluntary saving, will tend to be permanent only to the extent to which the savers continue to maintain the new high rate of saving even in face of falling rates of interest. But why should they? Why is it regarded as in any way reasonable to argue on the assumption that they will? There is no warrant for any such idea.

But of course Dr. Hayek does not mean that the entire burden of reducing prices will fall upon the rate of interest. He assumes that the return paid for the use of the 'original means of production' will be reduced to a sufficient extent, in conjunction with the fall in the rate of interest, to enable the costs of production to fall to the new level required for the re-establishment of equilibrium. Though he nowhere makes clear this absolutely vital link in his argument, he is in fact assuming throughout that not only the rate of interest, but every element that enters into the cost of production, is perfectly elastic. This assumption is expressed in the shortening of the line which represents payments for the original means of production by precisely the same amount as the base of the triangle, which represents expenditure on consumers' goods. Needless to say, if this assumption were true, costs would fall enough to offset any reduction in consumers' expenditure; for the costs would be only a redistribution of the sums spent by the consumers —which is what Dr. Hayek assumes them to be. But actually things do not happen like this. Many elements in cost are contractual, and have been fixed over long periods; and other elements are 'sticky', showing greater or smaller degrees of what is called 'rigidity'. Accordingly, if equilibrium is to be restored, this can be done only in two ways. Either the less rigid elements in cost must bear a disproportionate share in the decrease, or, despite the accession

of new capital, there must be a decrease in the quantity of goods produced below what could be produced with the available supply of capital, new and old, using the available supply of 'original means of production'.

The less rigid elements in cost are not always the same. The rigidity of wage-rates varies with the strength of Trade Unionism in the various industries and the nature of industrial legislation. The rigidity of new rents depends on the degree and strength of land monopoly in its various aspects. The rigidity of interest rates is greatly affected by the current scale of non-industrial borrowing, *e.g.* borrowing by Governments, and is not necessarily the same for different kinds of borrowers. Accordingly, there is no possibility of generalising absolutely about the effect which a forced reduction in costs, due to an increased rate of saving, will have on the rewards of the different beneficiaries of the industrial process. But clearly, to the extent to which any one group of costs is rigid, either the remaining costs must fall all the more, or the total reduction in costs must fall short of what is required to re-establish equilibrium on a basis of the full use of the old and new productive resources combined.

In resisting reductions in their money returns, the sellers of both land and labour are at a disadvantage because the supply of both these factors is relatively fixed. But landlords as a class have an advantage over labourers as a class in that rent contracts run for much longer periods than wage contracts. This does not protect the landlord who has to let out his land afresh; but it does mean that existing rent contracts represent an important rigid element in costs. Similarly, only the rates of interest for new money are elastic in relation to current business conditions; and interest on existing debts constitutes another even more important rigid element in the cost structure of advanced industrial economies. A limit will be set to current interest rates for new money by the elasticity of the supply of capital; and this will prevent the burden thrust off by the receivers of rigid incomes from falling on the owners of new

capital to the extent necessary to re-establish the postulated equilibrium.

What then will happen? The costs which count are of course the marginal costs, that is, the highest costs necessary to elicit the quantity of production that producers find it worth while to produce in view of the state of consumers' demand. Dr. Hayek appears to assume that these highest costs will appear among the users of the new supply of capital; for he tells us that the effect of the additional rate of saving will be to push capital into less remunerative uses. But is this really the case? Will not at any rate a large part of the new capital go into uses directly competitive with those to which the existing capital resources are being applied? And will not the consequences be that the new capital, being employed not in less, but in more remunerative ways, because of its ability to take advantage of the latest technical developments in the arts of production, will drive a substantial fraction of the existing capital resources out of business, by throwing them below the margin of productive efficiency? Of course, the first effect will be to compel the owners of old capital resources to cut their prices, in order to compete with the new, more efficient instruments of production; and this will react first on the dividends, as distinct from interest, they are able to pay to their shareholders, and, secondly, on the wages they are prepared to pay to their workers. At a later stage, if they are rendered insolvent and compelled to reconstruct, it will also react on their fixed contractual charges. But this will come later, if at all.

In these circumstances, prices to consumers will not in fact be so readjusted as to keep all the old, as well as the new, capital resources in use. Some firms will close their doors, and go out of business, without their plant being taken over and re-employed by other *entrepreneurs* who are able to buy it cheap. In fact, there may, under modern conditions, be a definite process of buying up firms in difficulties, in order to put them out of business, and so check the competitive price-cutting that would otherwise

occur. But even without this some firms will disappear, their size and number depending on the rigidity displayed by their costs in face of the lower level of consumers' spending.

If this happens to a considerable extent, the new rate of investment will not cause a proportionate addition to the total capitalisation of the economy. The more new capital is invested, the more existing capital will be destroyed. This will limit the quantity of additional goods coming on the market, or even perhaps, in particular cases, prevent there being any increase at all. This in turn will limit the fall in prices required to re-establish equilibrium, though the new prices will still have to be, on the average, lower than before for any given supply, in proportion as the consumers' expenditure has been reduced.

Clearly, how far new capital will drive out old capital resources, or how far it will be used to add to the total product, depends on the state of the technical conditions of production. If the new capital can be used to produce goods much more efficiently than the old, the proportion of old capital resources driven out of use will be very large; for there will be a large fall in marginal cost. If, on the other hand, the technical conditions do not offer prospects of large advantage to new capital, relatively few existing resources will be disused; for the owners of existing capital will be able, by cutting at the less rigid elements in costs, to remain in business at a lower level of selling prices. If, however, new capital has any substantial technical advantage over old, so as to be able to produce at a lower cost, it will be able to find fields for investment under more favourable conditions than are enjoyed by old capital, and will thus tend to enter into competition with old capital. Under these conditions, where the technical advantage is small, the largest fall in prices will tend to result, in the short run, from an increase in the rate of investment; for the new capital will come into operation without, at first, driving out much of the old. But in the long run the consequent larger fall in prices due to the greater output will

react on the older firms, so as to drive more of them out of business; and the small competitive advantage of the new capital will involve a lower rate of interest, and in fact cause a fall in the total flow of new capital into investment.

Thus, whether the technical conditions offer a large or small advantage to new capital over old, provided that they do offer some advantage, an increase in the rate of investment will tend to throw old capital out of use. This process of superseding old capital resources by new is, of course, up to a point the very foundation of economic progress. It is constantly going on, not only in the competition of one business with another, but within the internal economy of every progressive enterprise. It is but the ordinary business practice of writing off for obsolescence as well as depreciation writ large in the balance-sheet of the industrial system as a whole. Nevertheless, it is very possible under the conditions of capitalist industry for this process to be so carried on as to involve the economy as a whole in unnecessary loss; and this is most likely to happen when it comes about under the conditions which Dr. Hayek seems to regard as pre-eminently desirable — conditions which involve, as we have seen, a tendency for prices to fall faster than productivity increases, and therefore must involve the disuse of existing resources as a means of counteracting this tendency. For under these conditions, in which the fall in consumers' incomes is pressing towards a heavy fall in the prices of consumers' goods, the destruction of existing capital resources is likely to proceed too fast, so as to involve the writing off and disemployment of resources which it is well worth the community's while to go on using for a further period.

This situation would not arise, at any rate to the same extent, if the business costs and the social costs of production were the same. Nor would it arise to the same extent if the factors of production, other than the displaced capital resources, were perfectly transferable to other employments. For, if the remaining factors were fully transferable, they could be at once used to the full, in conjunc-

tion with new capital resources, up to the maximum of the available supply of new capital; and, so used, they would have a higher productivity than before, as long as any opportunities for technical advance still remained open. But in fact the other factors are very far from being transferable to this extent, so that serious and prolonged frictional unemployment of 'original means of production' may result from the disemployment of the capital resources in connection with which they have been in use.

Moreover, business and social costs do not coincide. When existing capital resources are disemployed, this process often involves the disuse of other capital resources which are usable only in conjunction with the displaced resources, and the creation of alternative new resources to be used in conjunction with the new instruments of production. If these supplementary resources figured as costs to the *entrepreneurs* using the old and new instruments of production, no complications would arise. But commonly they do not. The closing of a factory or a coal mine may pauperise a whole town or village, and destroy the value of the houses, shops, public utility services, etc., attached to it, while imposing on someone the need to supply new houses, shops, and services elsewhere, for use in conjunction with the new capital resources. This process may involve a great addition to social costs of production, without being reflected in *entrepreneurs'* costs at all. And a rapid rise in the rate of saving is calculated to create precisely the conditions which will lead to this type of social loss.

It is often argued that this is the price which has to be paid for industrial progress; and doubtless so it is, to the extent to which the rate and direction of investment in industry are to be regarded as factors beyond any collective control. But the realisation of the losses which may arise in this way should at any rate serve to make us cautious about accepting the view that *any* increase in the rate of investment is necessarily desirable from the economic point of view. It is argued, again, that undesirable investment will necessarily be checked by the fall in the rate of

interest which a rise in the rate of investment will involve. But this is manifestly not the case; for the fall in the rate of interest will be checked in proportion to the success of the new capital assets in driving old capital assets out of business. It is then argued that the extent to which the older assets will be driven out will depend on the degree of superiority of the new means of production over the old, and that accordingly the community will always benefit. This is true in the long run; but to conclude from it that there is nothing to worry about is to miss the point that the struggle between old and new capital totally ignores the *indirect* consequences of the supersession in causing frictional unemployment and destroying other capital assets such as those mentioned above.

Now, the destruction of old capital assets is likely in the long run to proceed furthest where the technical opportunities for increasing productive efficiency are greatest. For under these conditions the demand for new capital is most elastic, and the fall in the rate of interest in face of an increased supply least. If, under these circumstances, there occurs a considerable contraction in the money income applied to the purchase of consumers' goods, the new capital will be applied chiefly to supplant rather than to supplement the existing instruments of production. For more of the existing instruments will be driven below the margin of productivity. The new instruments of production will, however, tend, owing to their more capitalistic nature, to give employment to a smaller number of workers in relation to the volume of output. The consequent disemployment of workers will have the effect of reducing consumers' incomes of a sort which are spent largely on consumable goods; and this reduction will set up a further tendency to disequilibrium in the economic system. It is not necessarily more economic for more productive instruments of production to be employed, if the effect of employing them is to involve the community in additional charges, not represented in producers' costs, for the maintenance of unemployed workers.

Doubtless it will be answered that this situation will be put right as soon as wage-rates have been reduced to a new level low enough to cause the re-employment of the displaced workers, and that the competition of the labourers for jobs will, as wages fall, tilt the balance back in favour of the employment of additional labourers rather than additional instruments of production. It is admitted that this process of reducing wage-rates by competitive pressure is not easy to carry through, especially where Trade Unionism is strong and social services have been largely developed. But let us assume that wages have been reduced in this way, and see what follows. The reduction in wages brings about a further fall in money-costs, and thus enables goods to be cheapened. This seems to be what Dr. Hayek expects to happen, so as to bring the money-incomes dispensed to the 'original means of production' down to any point that the reduced level of consumers' money demand may require. In other words, he is again assuming that the incomes of the owners of 'original means of production' ought to correspond to the prices of the available output of consumers' goods. But, as we saw earlier, there is no real basis for this equivalence, which rests on the assumption that the recipients of interest save and invest, whereas the receivers of rent and wages spend, their incomes. He will, however, doubtless agree that to the extent to which these latter groups save and invest, there is no reason why wages or rents should fall in money amount, except to the extent to which the new conditions of production involve an increased lock-up of money in intermediate exchanges; and the reduction consequent on this lock-up will fall in part on the receivers of interest as well.

It will be argued that the fall in wages will affect not the size of the total wages-bill, but its distribution—by increasing the numbers employed by means of a given 'wages fund'. But Dr. Hayek clearly contemplates, apart from this, a fall in the total wages-bill corresponding to, though not necessarily of identical magnitude with, the fall in consumers' spending. If consumers' spending falls,

according to the triangle wages and rents must fall to a corresponding extent, as aggregates and not only as payments to each individual worker or landlord. Presumably Dr. Hayek does not really mean this; but this is what his diagnosis appears to involve.

If this fall were to occur, it would on the face of the matter re-establish equilibrium; but it would do so only on the assumption that the new higher rate of saving was permanently maintained. This, however, implies the continuous existence of openings for the investment of capital on the higher scale, under conditions technically favourable enough to admit of a continued reduction in prices sufficient to enable the goods produced with the aid of the new machines to be marketed, without driving an undue quantity of old capital resources out of use.

For it must be strongly emphasised that investment attains its purpose, and can be in the long run socially useful, only if it leads to the successful marketing of an increased supply of consumers' goods and in proportion to the magnitude of the increase. The demand for instruments of production, and for all intermediate goods, is a derived demand—derived from the final demand for consumers' goods. Investment that does not issue in higher consumption is sheer waste. But, in face of increased saving out of a fixed supply of money, it can issue in this way only if prices of consumers' goods fall faster than productivity advances.

Dr. Hayek will perhaps answer that this is the very point of his insistence that saving must be voluntary and not forced, because an increase in the will to save implies a willingness to accept a lower rate of interest, so that a balance will indeed be struck in such a way that the fall in interest-rates will enable costs to fall more rapidly than the efficiency of production advances, thus rendering possible a greater fall in prices, while saving will be checked by the fall in interest-rates precisely at the point required in order to avoid a piling up of productive resources that cannot find an issue in the successful marketing of con-

sumers' goods. This view would be plausible if all capital were new capital, governed by the current rate of interest, and if there were no existing instruments of production capable of being driven out of use by the competition of more efficient instruments purchased with new capital. But, in face of the existence of these factors, it quite fails to reflect the real situation. The old, rather than the new capital, feels the pressure of the new conditions; and, if the technical possibilities are favourable, the rate of interest on new capital may even not fall off at all.

This brings me to another of Dr. Hayek's assumptions. He seems to assume that an increase in the rate of saving will cause new capital to be employed in less productive uses than the capital already in being, or, as he puts it, to be applied to more roundabout forms of production than are remunerative when capital is less abundant. But in fact, as we have seen, the new capital is likely, under favourable technical conditions, to be applied to more rather than less remunerative uses than the old. It is true that, as the supply of new capital is increased, the marginal uses of it will be less productive than the marginal uses of a smaller supply; but it is by no means true that the marginal uses of the new capital will be less remunerative than the marginal uses of the capital already in existence. It is with these latter uses that the new capital will come into relation. The rate of interest for new capital will be lower than it would be if the supply were smaller; but it need not be any lower than the rates already in being for old capital. Whether it will be lower depends on the technical situation of the time.

The gist of the matter is that the rate of new saving has an upper limit of desirability determined by two factors—the possibility of technical advance in productive methods, and the *indirect* losses liable to be caused by the competition of new capital with old capital. The rate of interest is a wholly inadequate instrument for securing that the rate of saving shall remain within these desirable limits.

Let us come back now to another remarkable assumption

which Dr. Hayek appears to make. He holds that a change in the relation between spending and investment will tend to be permanent if it is brought about by an increase in voluntary saving, but not if it is the result of an increased supply of money in the form of producers' credits. I am not for the moment discussing his negative conclusion; but can his positive conclusion stand? He simply assumes an increase in voluntary saving, without discussing at all how or why it comes about. In a private capitalist economy, such as Dr. Hayek is discussing, an increase in voluntary saving can arise from any of three causes, or of course from a mixture of the three, or of any two. One is an increased psychological willingness to save—a change in the rate at which future goods are discounted. The second is a greater willingness to save on account of the offer of a higher inducement, that is, a higher rate of interest. The third is an increased ability to save, which will arise from the payment of higher incomes to those who receive incomes high enough to allow a surplus for saving.

Now, if the source of the additional saving is a greater psychological willingness, I agree that the change will have some elements of permanence. There will tend to be a lasting increase in the proportion of saving, but not to the full extent of the change in the rate at which the future is discounted. For, as Dr. Hayek points out, if the higher rate of saving causes the rate of interest to fall, as capital has to be pressed into less profitable uses, this fall in the rate of interest will in part offset the increased will to save. There will, however, be *some* tendency to permanent increase in the rate of saving, corresponding, if other things behave in the manner Dr. Hayek assumes—which I shall discuss later—to the change in the relative psychological valuation of present and future goods.

But the position is not the same if the increased rate of saving is due in the first instance to either of the remaining causes. If it is due to higher interest-rates, the additional saving will bring these rates down, perhaps to the old level. And if it is due to a change in the distribution of incomes

to the advantage of the richer as against the poorer classes, the outcome will depend on the permanence of this change in the distribution of incomes. Dr. Hayek is doubtless mentally ruling out the two latter causes, because he is assuming a condition of things in which all incomes represent the marginal productivities of the various factors of production and arguing from a basis of static equilibrium, which presumably includes the idea of a static rate of interest, and a static distribution of incomes between the various classes of recipients. But in a Society in which incomes are affected by taxation and social legislation, as well as by Trade Unions and capitalist monopolies, these are certainly not assumptions which can be made in practice. Moreover, even apart from these factors, technical conditions may arise which temporarily raise or lower the demand rate for new, and the yield on already invested, capital, and thus temporarily affect the willingness or the ability to save voluntarily, without any assurance that the change in the rate of voluntary saving will be lasting.

I am accordingly compelled to reject Dr. Hayek's assumption (which he nowhere attempts to argue) that changes in the rate of voluntary saving will tend to be permanent, and therefore serve, unlike 'forced saving', as the basis for a new economic equilibrium as soon as the necessary readjustments of the industrial system have been made. This may happen; but there is no guarantee at all that it will. In reality, there is more likely to arise a conflict between the rate of interest needed to maintain the higher rate of saving and the necessity for reducing prices enough to allow the lowered consumers' income to buy the increased supply of consumers' goods which the higher rate of saving has enabled the economic system to produce; and this conflict may easily lead to a socially undesirable supersession of existing productive resources. Incidentally, it should be observed, there is no evidence at all that, in highly developed communities, the proportion of saving needs to expand in order to allow of the fullest technical progress consistent with equilibrium in the economic system

on a basis of full employment of the factors of production. Probably the rate of saving needs, in such communities, rather to decrease, if waste is to be avoided and equilibrium maintained, unless a large part of the saving is absorbed by public investments, not designed to yield a direct economic return.

This brings me to a further ambiguity in Dr. Hayek's presentation of his case. I have so far not questioned his procedure of lumping together, as contrasted with consumers' goods, all types of intermediate goods, whether they consist of instruments of production or of goods in stock or in process of manufacture. But the distinction between goods of these two types is important. Clearly, more capitalistic methods of production do commonly involve an increased use of instrumental goods—fixed capital, as they used to be called—and probably, though not necessarily, an increase in the amount of money currently applied to the purchase of such goods; but it is by no means so clear that they need involve a larger lock-up of money capital in goods in stock or process, or a larger physical lock-up in proportion to the volume of final consumers' goods. That they often appear to do this at present is largely due to restrictive tendencies, such as the holding of involuntary stocks, which arise from the fact that the economic system is not in equilibrium. Technical progress can be made by reducing the need for holding large stocks —working capital—and often is so made. Nor is there any theoretical reason why the economy in working capital should not offset the increase in fixed capital, so that the total money 'capitalisation' need not increase any faster than the total price of the output of consumers' goods. What is called 'Hand-to-Mouth Buying' had been making rapid progress in the years before the slump; and there is room for great economies in working capital by means of improved methods of marketing in many trades.

These tendencies, obviously, make for a smaller ratio of investment to spending; and Dr. Hayek may contend that, to the extent to which this is so, his argument is not

affected; for he begins by assuming an increased rate of investment. But he appears to assume without question that the advance of technical productivity does involve a higher proportion of money investment to consumption income; and this is the assumption which I am concerned to deny.

Moreover, Dr. Hayek's division of all goods into intermediate goods and consumption goods is misleading. What, in this dual classification, is the place of durable consumption goods such as houses, roads, and many public and private utilities which yield up their values directly over a long period of time? I presume they must be classified as 'consumption goods'; but clearly they are entitled to rank as embodiments of saving and investment. It is to goods of these classes that an increasing amount of the total saving tends under modern conditions to be directed. But such saving does not necessarily tend to make the processes of production more 'roundabout', or even more capitalistic in any sense.

Let us come back to the triangle. We have seen that the vertical line does not necessarily tend to grow longer as production becomes more capitalistic, whether it be regarded as standing for the length or the roundaboutness of the productive process. We have seen further that the slanting line need not either lengthen or bulge, so as to increase the area of the triangle representing the lock-up of capital in intermediate goods. It follows that there is no necessary reason, even on the assumption of a fixed supply of money, for a shortening of the line at the base, in order that the full advantage consistent with equilibrium may be taken of the opportunities for technical advance. Of course, if consumers do both persistently *and increasingly* save a larger proportion of their incomes, no matter how low rates of interest fall, capital will be forced into less and less productive uses; and this process can go on as long as people can continue to invest in new machines for the purpose either of leaving them, or some of the existing machines, idle, or of selling an ever-increasing product at a price

continually falling faster than the cost of production. But, unless they are to do this, which is clearly the act of madmen, the limits to the desirable shift in the relative rates of saving and spending are, in industrialised countries, fairly narrow. I am not here discussing the problem of foreign investment, which is not raised by Dr. Hayek's argument. Nor am I denying that non-remunerative investment in social services can be pushed to any point a community may think fit to finance out of the proceeds of taxation.

There is a further point about the triangle which seems to merit attention. As we have seen, Dr. Hayek, in order to simplify his presentation, has left out interest on capital. According to his presentation, all the payments made at the successive stages of production are payments for the 'original factors of production', which he explicitly defines as land and labour, to the exclusion of capital. These payments are then assumed to add up to the same amount as the value of the entire supply of consumers' goods. In other words, it is assumed that all payments made for land and labour will be used in buying consumers' goods, and all payments for capital in buying intermediate goods. There is clearly no warrant for this assumption, as I presume Dr. Hayek would readily admit. It is, however, of importance; for, when Dr. Hayek shortens the base of his triangle (*i.e.* the money-value of the supply of consumers' goods), he has also, in order to preserve the balance, to shorten proportionately the value of the payments made for the use of land and labour. In other words, he appears to assume that rent and wages fall, in order to allow of the payment of more money in other forms. He also assumes, as we have seen, a falling rate of interest, due to the pushing of investment into less remunerative fields by the increased supply of capital. I am not sure whether the fall in the rate of interest is supposed to be just large enough to reduce the total money-income of the capitalists to precisely what it was before, despite the increased amount of capital invested; but if this is so the released money represented by the decrease in consumers' spending must go, not to the

capitalist as against the landlord and the wage-earner, but in other forms of intermediate payments required by the increasing roundaboutness of the productive process. If, however, the productive process does not become more roundabout as it becomes technically more advanced, there is no such need as Dr. Hayek supposes for the sums paid out in rent or wages to fall, though wage-rates will presumably tend to fall if the absolute number of wage-earners increases. I am assuming that the quantity of land remains constant, and not pausing to argue that rent will be affected by the changing opportunities for the profitable use of land which different adjustments of the productive system will afford.

But is not this sharp distinction, implied in the triangle, between the rewards accruing to the owners of land and labour on the one hand, and the owners of capital on the other, highly misleading? Capital, when once it has been invested, becomes a means of production differing in no essential particular from land, with which it is indeed often inextricably combined. Dr. Hayek's triangle, if it were logically drawn, ought to include at the top, not only the payments made for land and labour, but also those made for the use of the existing durable instruments of production and for all working capital locked up in intermediate goods. In other words, it ought to include interest, as well as rent and wages. But, if it did this, it would be impossible for it to present that specious balance which it now has, by making the value of consumers' goods seem to correspond to the value of the original means of production employed. For clearly rent + wages + interest (including salaries with wages, and profits with interest for this purpose, as we must on Dr. Hayek's assumptions) will add up to more than the value of the current output of consumers' goods, since they will have to suffice to buy the current output of new capital goods as well. Only on the quite unwarrantable assumption that all the interest (or an equivalent sum) goes to buy capital goods, while all the rents and wages (or their equivalent) go to buy consumers'

goods, does the specious balance of the two lines exist. What really balances, under conditions of equilibrium, is the total income on the one hand and the total supply of finished goods and services, including both capital goods and consumers' goods, on the other, additions or diminutions in the stocks of unfinished goods being treated for this purpose as added to or subtracted from the total output of capital goods.

How far does this examination of Dr. Hayek's triangle serve to invalidate the conclusions which he draws? It does not directly touch at all his conclusion that forced saving, in the form of an additional supply of money injected into the economic system as producers' credit, at a time when the system is in equilibrium and all the factors of production are fully employed, will serve to upset the equilibrium of the system. But it does cast grave doubts on his opposite contention that a change in the relation between spending and investment will have no more than a temporary disturbing effect, provided that the amount of money remains unchanged. An existing equilibrium may be upset by a change in the balance of expenditure on different classes of goods, even if the change is not due to a change in the supply of money; and accordingly Dr. Hayek, even if he has pointed out one of the dangers of inflation, has not shown that abstention from an inflatory policy will suffice to ensure equilibrium in the economic system.

This brings me back to the question whether, as Dr. Hayek seems to assume, equilibrium can be reached and maintained at *any* relative level of investment on the one hand and spending on consumers' goods on the other. I do not believe that it can; for I believe that, under a capitalist economy, the limit to the rate of investment compatible with equilibrium is set by the current technical conditions of production. Let us recall to mind that, in order that equilibrium may be secured, it is necessary for an increased rate of saving to bring about a fall in costs of production, and correspondingly in prices, large enough to

enable the reduced money-income available for spending on consumption goods to buy, not merely all the consumption goods that were being bought previously, but also the additional supply made possible by the aid of the fresh capital directed to investment—less such goods as the driving of old capital resources out of the market causes not to be produced. Whether this can happen will depend on the availability of new forms and instruments of production capable of being so applied as to bring about the requisite fall in costs—in other words, on the contemporary technical conditions. It is true that, if the technical conditions are unfavourable, the increased supply of consumers' goods will be less than it would be if productivity could be increased to a greater extent. But at the very least the reduced amount of consumers' money must buy as many goods as the larger amount was buying before, and *some* more. For we need not take account of the situation in which an increased application of capital lastingly decreases the total supply of consumers' goods.

Is there any assurance that this can happen in face of a large shift in the rate of saving, unless the technical conditions are highly favourable to the use of additional capital in production, or that it can happen even then without causing very large indirect losses? Dr. Hayek can doubtless argue that the rate of interest offered for the additional capital measures its estimated productivity, and that accordingly an increase in the rate of saving will not arise except under favourable technical conditions. But this is not the case, if the increased saving is the result of a shift in the psychological preference of the income-receivers for future as against present goods; for such a shift is not a result of the rate of interest, but, presumably, of a spontaneous change of values on the part of the income-receivers. It is clearly possible for these, if they act in this spontaneous way (and only if they do so act are there reasons for expecting the shift to be lasting), to shift their preferences even at a time when the technical conditions for the employment of additional capital are adverse.

Nor is this all. Dr. Hayek tends to speak as if the economy in production achieved by an additional application of capital could be at once passed on undiminished in the form of lower prices. But, as we have seen, this is very far from being the case. The new capital will be used largely in conjunction with old capital borrowed at a contractual rate higher than the new rate to which the greater plenty of capital forces down the rate for new money; and the total reduction in *capital* costs (apart from other elements in cost) will depend on the relative amounts of capital employed at the old and new rates at the margin, and on the difference between these rates. It is of course true that the possibility of more economical production by new methods will drive a certain amount of the old capital out of use, and lower the return to some of the equity owners of the old capital assets; but, to the extent to which the prices at which goods are sold must cover the costs of the marginal producers, this will not invalidate my point, which is that prices will fall by less than the reduction in costs which can be made by the most efficient producer using only the best methods and getting his capital at the cheapest rate. Nor do I need to remind Dr. Hayek that a reduction in manufacturing costs does not necessarily, or usually, carry with it an equal or proportionate reduction in the retail prices of consumers' goods. Yet it is in these retail prices that the fall must occur if equilibrium is to be restored and maintained at the new relative rate of saving and spending.

It is evident that a high rate of saving produces a large part of its effect not in adding to the total capital equipment of an economy but in driving out of the field of productive use existing capital assets which it causes to be superseded by more efficient instruments of production. The net saving, or investment, of the economy is thus very much less than the amount withdrawn from spending on consumers' goods. This reduces, it is true, the amount of the additional consumers' goods which the reduced consumers' spending has to avail to buy, and thus mitigates

the fall in prices which is required if equilibrium is to be restored. This process is indispensable up to a point; but, pressed beyond that point, it may involve a total economy in disastrous losses and prolonged disemployment of the factors of production.

So far, I have been trying to show that Dr. Hayek's remedy of a stable supply of money is not a guarantee of equilibrium in face of a changing balance between spending and investment. But what of his other contention, that any change in the supply of money, except certain downward changes which he seems in his closing chapter to regard as desirable, is certain to introduce disequilibrium into the economic process? This is Dr. Hayek's case against inflation, to which all the rest of his argument is in fact leading up.

First, let us take Dr. Hayek's view that there are circumstances in which the supply of money ought to be reduced, but apparently none in which it ought to be increased. This seems to be an astonishingly illogical view. Apparently if the amalgamation of capitalist businesses on vertical lines reduces the number of capitalistic stages involved in the productive process, so that goods exchange for money a smaller number of times, and the lock-up of money in intermediate transactions is thus reduced, there ought to be a corresponding decrease in the total supply of money. If, on the other hand, the growing roundaboutness of production increases the number of intermediate exchanges, there ought not to be any increase in money-supply, but rather a shrinkage of the money-income expended on consumers' goods. Why? If money is to be decreased in the one case, why should it not be increased in the other? Dr. Hayek argues that an increase in money-supply, even in these circumstances, will lead to disequilibrium. Will it? And, if it will, will not a decrease in the opposite circumstances also lead to disequilibrium? If there is a reason for this distinction, it is not made plain: nor can I imagine what it can possibly be.

The main question, however, is whether an increase in

the supply of money will lead to disequilibrium in all circumstances, or only in some. Dr. Hayek's contention, which is at this point very difficult to follow, seems to be that it will in all cases. He takes two opposite cases—additional credits issued to producers and additional credits issued to consumers; and he argues that both will throw the economic system out of balance.

Let us be clear at the outset that Dr. Hayek's argument starts out from the assumption that, to begin with, the economic system is in equilibrium, on a basis which allows all the 'original means of production' to be employed. There is no idle land or labour to be brought into use; and accordingly an additional supply of money can operate only by altering the use made of the original means of production, and not by calling additional original means into employment. His argument might therefore hold good on the basis of his assumption, without being valid for an economy which was not in equilibrium, and did possess unemployed 'original means of production'.

Is it, however, valid, even on his own assumption? Surely his examination of the two polarised cases of additional credits to producers and to consumers respectively obfuscates the real situation. The conditions which he assumes to exist are those of an increased lock-up of money in intermediate transactions. If these additional transactions are financed with the aid of new money, and no others, why should any disequilibrium arise? Is it because he assumes that the additional credits will necessarily be paid away to final recipients of income, who will then be able to spend them on either capital goods or consumers' goods in finished forms? If this is assumed, of course the effect is to increase total money demand for finished goods, and therefore to raise their prices above the old level, at any rate for a time. But need additional intermediate credits ever be paid away in this form, if they are required only to finance an additional volume of intermediate exchanges? I am quite unable to see why they should.

In effect, here again Dr. Hayek has fallen into a confusion through lumping together, under the one heading of 'intermediate goods', both unfinished goods changing hands at successive stages in the course of production and instruments of production in the form of finished capital goods. If finished capital goods are bought out of new money, created as an addition to the previous supply, the consequence is clearly inflationary. But this is not true if additional money is applied to meet a situation in which the number of exchanges of unfinished goods in process has increased. There is nothing even remotely inflationary in an increase in the supply of money for this purpose, nor has it any tendency to set up conditions of disequilibrium.

It is, however, as we have seen already, very doubtful whether an advance towards more capitalistic methods of production need, on balance, involve an increase in the number of intermediate exchanges. It may even involve a decrease—which is the tendency under a more rationalised capitalistic structure of production and marketing. Accordingly, while Dr. Hayek's view is at this point demonstrably wrong, the refutation of it by no means justifies the conclusion that the supply of credit available for intermediate uses ought to be increased, unless it can be shown that the processes of production are actually becoming more roundabout in such a sense as to involve a larger number of money stages. For Dr. Hayek is clearly right, on his assumption of an initial equilibrium, in holding that the creation of additional money for the purchase of new finished instruments of production will be inflationary in its effects. Equally, of course, he is right, on his assumption, in regarding as inflationary any additional issue of purchasing power to consumers out of newly created money.

Dr. Hayek does not, indeed, show that all inflation necessarily leads to disequilibrium. What he does show is that, given equilibrium and full employment to start with, the pumping of additional money into any one part of the economic system will disturb the structure of demand, and upset the balance of relative prices. He does not show that

this would happen if the new money were pumped simultaneously, in the appropriate doses, into all parts of the economic system. If that could be done, the effect would be a rise in prices all round, without disturbance of balance. But it is, of course, practically impossible to pump in new money in this way, because of the very different rigidities of different parts of the economic structure, and the comparative ease and difficulty of pumping the new money into its several parts. We may therefore agree that, if balance exists at the outset, the pumping in of new money is bound in practice to lead to disequilibrium.

This is, of course, a very important conclusion; for it is fatal to the numerous projects of perpetual stabilisation of prices that have been of late years so fashionable. I agree entirely with Dr. Hayek's attack on these projects, and hold that there is a strong presumption, if a satisfactory condition of equilibrium already exists, in favour of allowing prices to fall gradually as productive efficiency increases, so that a rising standard of life is achieved by means of falling prices rather than of increased money incomes. I should probably differ from Dr. Hayek in my definition of a satisfactory condition of equilibrium; for I do not hold that the distribution of incomes in the community can best be left to the play of the law of marginal productivity, or that full employment of the original means of production is the only condition required for satisfactory equilibrium. But that is another issue, which I have no space to discuss here. I do agree with him that, given a satisfactory equilibrium as a starting-point, it is the appropriate economic policy in a capitalist Society, which alone is under discussion according to the terms of the argument, to allow prices to fall as efficiency rises, rather than to increase the supply of money in order to keep prices stable. For I hold, as emphatically as Dr. Hayek, that relative price levels for different kinds of goods are of primary importance, and that any attempt to keep the 'general level of prices' stable is liable to introduce serious disequilibrium in relative prices.

I do not, however, follow Dr. Hayek in regarding the concept of a 'general level of prices' as wholly unreal or irrelevant. It cannot be so dismissed, because of the existence of large masses of debt incurred at fixed interest over a long period. For this burden of debt introduces an important element of inelasticity into the capital cost of production, and may greatly affect marginal costs. But this point also I lack space to pursue in this essay; for it does not arise directly out of the 'triangle', with which I am mainly concerned.

As we have seen, Dr. Hayek's demonstration of the unbalancing effects of an infusion of new money, subject to the corrections already made, holds good only on the assumption that, before the new money is created, equilibrium exists in the economic system. Does his analysis throw any light on the policy which ought to be followed when the initial position is one of disequilibrium, and there exist unemployed 'original means of production' — and also, probably, unemployed capital resources as distinct from money?

Dr. Hayek would, I think, argue that the effects of monetary interference in such a situation are so difficult to regulate that the only sound course is to do nothing, and to await the return of equilibrium by the erosion of 'natural' economic forces. But this conclusion does not follow from his argument; and it is a long step from saying that monetary intervention is undesirable when equilibrium already exists to holding that it must not be invoked to restore equilibrium when it is absent. The case for such interference is, at any rate on the surface, strong. For, in face of a large rigid debt structure, a considerably rigid system of distributive costs, a somewhat inelastic rate for bank advances, a by no means completely elastic rate of long-term interest (complicated by Government borrowing and by the international mobility of money), and a wage-system of very varying elasticity in different trades, the process of resuming equilibrium by mere abstention from interference may be so painful and protracted as to

threaten an economy with utter collapse before it can be carried to its appropriate end. It may involve wholesale bankruptcies and repudiations, bitter industrial struggles, the destruction of vast social assets invested in public utilities, enormous expenditure on the maintenance of unemployed workers for many years on end; and perhaps revolution. An economist in his study may be able to contemplate dosing an economy with such medicine. But the economy belongs to men and women, who will be certain to revolt against the treatment, whatever the economist says in justification of it.

If, then, a situation exists in which prices are definitely below the level at which it is worth the while of *entrepreneurs* to employ all the available means of production, and if costs can be reduced to a level consistent with full employment only by methods which are politically and humanly impracticable, what is to happen? What will happen is that the supply of money will be increased, in an attempt to raise prices to a level consistent with a fuller employment of the means of production.

Dr. Hayek does not deny that this policy can for a time cause more factors of production to be employed; but he asserts that it will inevitably lead to a new disequilibrium in the economic system. At least he suggests this, if he does not assert it positively. Why does he hold that this effect will be produced? Because the relative prices of different classes of goods will be disturbed. But what if such a disturbance is precisely what is needed in order to restore equilibrium, because at the outset relative prices are out of balance? Cannot the new money be used to restore the lost balance, and the creation of new money be stopped at the point at which the balance has been restored?

We are starting, be it remembered, from a situation in which unemployed factors of production exist. We can take it as certain that they exist to some extent in nearly all industries, but most extensively in the industries which produce capital goods. For industrial depression, for reasons that are obvious and well known, always reacts

most seriously on the output of the industries producing investment goods. Surely, then, the natural step is to create an additional demand for the products of these industries. This, however, cannot be done in the first instance by stimulating the production of additional capital goods for use in industries catering for the ordinary consumers' market; for the demand for new capital goods cannot arise on a large scale in these industries until the existing plant has become more fully employed. It is accordingly necessary to find means of increasing activity in the constructional industries in such a way as not to drive existing productive resources out of use.

The answer to this problem lies in a policy of public works, financed directly with the new money. If this is done, a large part of the new money paid out for public works will of course speedily reach the pockets of persons who will spend it on consumption goods; for when money is once paid out it goes on circulating from hand to hand. All industries will thus receive a stimulus; but the stimulus will be greatest in the constructional trades, and will be passed on thence to all other industries, but especially to those producing consumption goods. This corresponds with the needs of the situation. The constructional industries need the largest stimulus, and get it. But all industries need some stimulus, and are able to increase their output first by re-employing their own disemployed resources, and secondly by taking in new capital and so employing additional factors of production.

It is objected that the stimulus to the constructional trades, and therewith the indirect stimulus to industry generally, will cease as soon as the expenditure of public works stops, and that in the meantime the constructional industries will have been unduly enlarged. But, in the first place, the output of the constructional industries can be expanded more largely than that of others without considerable new investment in fixed capital by the full use of their existing productive resources; and secondly the indirect stimulus to the consumption industries will create a

demand from them for new capital goods, so that this demand will replace the demand created by the public works programme. The existence of large unemployed resources in the constructional trades will prevent the additional demand for their services from raising the prices of their products beyond the desirable equilibrium point, while the less concentrated character of the increased demand for consumers' goods will prevent an excessive rise in their prices. If the policy is rightly proportioned, so as to taper it off and stop it at the point at which the nearest practicable approach to full employment of productive resources has been achieved, there is no reason why it should not be effective, not only in increasing total employment of resources, but also in redressing previous disparities in relative prices. It will achieve these results only if it be well and courageously managed; but if it is so managed there is no reason why it should not succeed.

Dr. Hayek, however, thinks that it will not be well managed. He is so sure that those who attempt monetary management will make a mess of it that he is determined above all else to scare them off. Hence the 'triangle' and the warning that he professes to base upon it. But in fact, as I have tried to show, the 'triangle' is a misshapen product of confused thinking; and even where the deductions which Dr. Hayek draws are correct, as certain of them are, they prove the unwisdom of creating new money not absolutely but only when equilibrium exists and is being successfully maintained without this expedient. Dr. Hayek's case is sound at many points; but where it is sound it is not based on the triangle.

IX

SOCIALISATION[1]

THE purpose of this essay is not to discuss the merits or demerits of socialisation itself or of any particular form of socialisation, but only to elucidate the meaning of the word. For although it may be and usually is impossible in economic thinking to reserve a word for a single and unequivocal meaning, it is of the greatest importance, if we must use a word in more than one sense, to be conscious what the different senses of it are and in what sense it is being employed in any particular context. Failure to make unequivocal use of economic terms has been responsible in the past for a great deal of confused thinking; and to-day, when the word 'socialisation' is being flung about in so many controversies and used in so many different though related senses, it is of paramount importance that we should be as clear as possible in our minds what these different meanings are and should endeavour in our thinking to keep them securely apart.

The word 'socialisation' is now most commonly applied to the bringing of industries or services previously in private hands under some form of public ownership and control. This, however, is not the sense in which it was first widely used in economic and sociological discussion. For there is a more inclusive meaning in which it has been largely employed in sociological writings from the time of Karl Marx; and it will be best to begin by giving an account of this sense of the word before we come to its current use in relation to plans for the reorganisation of industry under the auspices of the State.

Marx, in his account of the historical evolution of Society, regarded the characteristic of the modern develop-

[1] Based on an article published in the *Encyclopaedia of Social Sciences.*

ment of the productive powers as the progressive 'socialisation' of the processes of industry and manufacture. As industrialism advances, it involves a rapidly growing degree of co-operation among the individuals engaged in production. The division of labour is the first form of this co-operation, which proceeds to a further stage with the subdivision of labour in 'manufacture'—that is to say, capitalist organisation of hand-work before the days of machinery—and to a further stage still in the 'machinofacture' which begins with the Industrial Revolution. The workman under both manufacture and machinofacture is increasingly converted from a complete producer with a product of his own into a 'detail labourer', whose work possesses significance only in relation to a co-operative group; while even the separate factories and industries built up on a basis of this productive co-operation also come to possess significance only in relation to the wider interchange of products in the economic system as a whole. In the last resort Marx thinks that the capitalist system in its final and absolute phase can best be regarded as producing only one congealed mass of commodities possessing a single unified value derived from the combined labour of a single mass of workers whose activity has been completely socialised. This growth of socialisation in the productive processes is forced upon Capitalism by the inherent necessities of its own internal processes of development, and is at the same time the means of carrying Capitalism to its ultimate point and of bringing about its supersession by a Socialist system in which the class divisions characteristic of capitalist Society will disappear in a classless Society corresponding to the completely socialised character of the productive system.

The word socialisation is, however, more commonly employed nowadays, not in this wider sociological sense, but in certain narrower senses relating to the actual forms of industrial ownership and control. In this connection it is used in at least three distinct senses, which are, however, often confused. In the first place it is used loosely

as equivalent to nationalisation—that is to say, the assumption by the State of the ownership of industry, whether this assumption comes about by direct expropriation of the capitalists or is accompanied by some form of compensation. In another sense the word socialisation is sometimes contrasted with nationalisation, as it often was among pre-war British Marxists, who used it to mean nationalisation without compensation, whereas they regarded the word nationalisation as identified with the piecemeal methods of nationalisation with compensation associated with the British Labour Party. In yet another sense the word socialisation has been used to mean something wider than nationalisation, as including forms of public or quasi-public ownership other than direct ownership by the State. Thus before the war it was often used to include municipalisation as well as nationalisation, and sometimes in a wide enough sense to include co-operative ownership, regarded as a form of social ownership complying with the requirements of a socialised economic system. Since the war it has been used also to include forms of quasi-public ownership of industry not directly by the State, but by public Boards or Corporations established under the authority of the State, and amenable to public control and regulation.

With the growing controversies concerning the forms of Socialist ownership and control of industry this last sense of the word has become particularly important. Its German equivalent *Sozialiserung* was widely used in connection with the discussions of the post-war Socialisation Commissions in both Germany and Austria. Both the German Social Democratic leaders headed by Karl Kautsky and the Austrians headed by Otto Bauer were opposed to direct State management of industries and advocated the placing of socialised industries and services under some form of representative council or commission including, side by side with State nominees, representatives of the consumers and producers, and sometimes also of the technical and managerial personnel. This question was

widely debated by the first German Socialisation Commission in 1919, and this body worked out a form of organisation for the mining industry based on tripartite control by representatives of the workers, the management, and the community. The second German Socialisation Commission under Rathenau's influence proposed a commission of four parties, including representatives of the managers of local mines, the workers and officials, the consumers, and the State. Meanwhile, other German writers, notably Rudolph Wissell and Otto Neurath, worked out a plan known as the 'Economic Scheme' for the social control of all industries in accordance with a planned arrangement of production and distribution, but without actual public ownership. Kautsky, advocating public ownership but not direct State control, powerfully criticised this plan in his book *The Labour Revolution*.

Meanwhile in France the Confédération Générale du Travail had worked out its scheme of *nationalisation industrialisée*, which proposed to exclude the State from any actual share in the control of industry and to hand over its conduct to representative organisations of the producers, technicians, and managers, under a form of public control. Somewhat earlier the Guild Socialists in Great Britain had worked out even more far-reaching schemes for the complete functional control of socialised industries and services; and some echo of Guild Socialist proposals was heard in the United States in such projects as the 'Plumb Plan' for the reorganisation of the American railroads, drawn up by the industrial engineer, Mr. Glenn E. Plumb.

The Guild Socialists in Great Britain had begun working out their doctrines even before the outbreak of the war in 1914; and Mr. S. G. Hobson and Mr. A. R. Orage published in 1914 their volume *National Guilds*, which laid the foundation of the movement. This book was based on a series of articles published in the *New Age* during the two previous years. According to the plan laid down in *National Guilds*, each industry was to be reorganised as a self-governing

public service corporation established under a charter from the State, which was thereafter to keep out of the industrial field save as a final co-ordinating and chartering authority. Promotion to leadership was to take place within the Guilds themselves; and the actual workers were thus to be made responsible collectively for the choice of their leaders and for the successful operation of the enterprises in which they were engaged. On the foundations laid by Mr. Hobson and Mr. Orage the National Guilds League, founded in 1915, proceeded to elaborate the Guild Socialist doctrine. One school of Guild Socialists remained faithful to the plans laid down in *National Guilds*, whereas another school advanced further in a Syndicalist direction by suggesting that the Guilds would come together in a self-governing Guild Congress which would take over the co-ordination of the various industries and services and thus complete the structure of industrial self-government, leaving to the State only the function of negotiating as an equal with the Guild body as the representative of the consumers' interests. This school of thought subsequently went further still, envisaging the entire disappearance of the State as a sovereign authority and the partition of sovereignty among a number of co-ordinated and co-equal authorities representing the community in its various functional aspects. The adherents of this school drew a distinction between the 'consumers' and the 'public', and envisaged the creation, partly on the basis of the municipal authorities and the Co-operative movement, of an all-embracing structure of consumers' organisations working in close conjunction with the National Guilds of producers, the final authority in the community as a whole resting with some sort of communal body built up on a basis of representation of the various functional groups. At the other end of the scale the Guild Socialists insisted strongly on the importance of local control in the workshops, so that the entire structure of industry should be throughout democratic and self-governing in the most complete sense.

Undoubtedly these Guild Socialist projects exercised a

powerful influence on the thought of the Trade Union and Socialist movement in Great Britain. They were not accepted as a whole, but many elements derived from Guild Socialism passed over into the approved plans not only of the leading Trade Unions but also of the Labour Party and of the Socialist bodies in the years immediately after the war. For example, the Miners' Federation of Great Britain worked out and placed before the Coal Commission of 1919 a detailed project for the socialisation of their industry. This plan involved complete public ownership of the mines and their administration under the auspices of a National Mining Council of which the Miners' Federation was to appoint half the members, the other half being appointed by the State to represent not the consumers or the general public but the technical and administrative grades concerned with the industry. There was also to be under this scheme a Coal Consumers' Council; but this body was to be advisory and was to have no actual managerial or administrative functions. It is noteworthy that this scheme of 1919 embodied a complete change of attitude on the part of the miners, who, in their pre-war Bill of 1912, had demanded the nationalisation of the mines on the traditional lines of handing them over to the administration of a Government department without any special provision for workers' control or for the Trade Unions to take a part in the management.

The National Union of Railwaymen also worked out in less detail a plan for railway nationalisation on a basis which was to give the railway Trade Unions at least half the seats on the proposed managing body; and in the scheme for the co-ordination of the railways put forward on behalf of the Coalition Government by Sir Eric Geddes in 1920 it was proposed to give the workers representation on the directorates of the grouped main line railways, which were, however, under this scheme to remain under private ownership. This offer was rejected by the railway Trade Unions, which were not prepared to participate in management under private ownership and preferred the scheme for

negotiating Whitley Councils and for a statutory Wages Board, subsequently embodied in the Railways Act of 1921.

It was in connection with the railways that the first sharp difference of opinion on the subject of socialisation appeared within the Trade Union movement in Great Britain. While the National Union of Railwaymen, by far the largest Union in the service, advocated a representative council on which the Trade Unions would have at least half the seats, the Railway Clerks' Association, which enrols the clerical and supervisory grades, advocated the socialisation of the railways in respect of ownership, but the placing of them under a full-time expert board of a non-representative character. This controversy came again to the front during the tenure of office of the second British Labour Government between 1929 and 1931, in connection with Mr. Herbert Morrison's Bill (which has since become an Act as modified by the subsequent National Government) for the socialisation of London passenger transport. Mr. Morrison proposed to place the co-ordinated passenger transport service, which was to pass into public ownership with compensation to the previous owners, under a salaried expert board, and rejected the demands of the Trade Unions concerned for representation on this body, on the ground, *inter alia*, that if the Trade Union claim were admitted, it would be impossible to exclude claims for representation from other groups, such as the municipalities, and even perhaps the former shareholders. Over this issue an active conflict arose inside the British Trade Union movement, and at the Labour Party Conference of 1932 further proposals for the socialisation of the Electricity and Transport services were referred back for reconsideration in the light of the Trade Union demand for representation upon the administrative boards.

It is, however, clear that this controversy applies only to the question of direct workers' representation on the managing bodies and not to the proposed form of socialised undertakings in itself. It is now generally accepted among Socialists alike in Great Britain, Germany, and France that

the actual conduct of socialised industries and services should in most cases be entrusted, not to Government departments, but to special *ad hoc* boards or commissions set up under the authority of the State. It is a moot point how far these boards or commissions should be representative of the actual workers engaged in the various services, or of the consumers, or of any other special groups, and further how far they should be amenable to political control. On the first point, British opinion has commonly rejected the plan, favoured by the German Socialists immediately after the war, of giving representation to consumers' groups upon the managing bodies, on the ground that boards consisting partly of producers' and partly of consumers' representatives would be likely to take up unduly sectional points of view and to prove inefficient in the business of day-to-day management. The Trade Unions continue to press hard for direct producers' representation on the boards, but in some quarters a distinction is drawn between two bodies—a small, full-time managing board of experts formed on a non-representative basis, and a wider council or commission of part-time members, with power to override the smaller board in matters of policy, on which the workers would be strongly represented. These two bodies would correspond to some extent to the Board of Directors and the Council of Oversight of a German company.[1]

On the question of political control there have been strong differences of opinion. The Socialists are for the most part in favour of the appointment of managing bodies by the State, even if the State acts to some extent only as a ratifying body for nominations made by outside groups. The State, it is held, should have the right of ultimate appointment and dismissal. Most Socialists also hold that the boards or commissions of socialised industries ought to be responsible to a Minister and to the Cabinet, especially on the ground that this is necessary if socialised services

[1] See my essay on *The Essentials of Socialisation*, in my book, *Economic Tracts for the Times*, and the pamphlet, *Workers' Control and Self-Government in Industry*, edited by me and Mr. W. Mellor (New Fabian Research Bureau).

are to be brought together as parts of any comprehensive national economic plan. Non-Socialists, on the other hand, generally wish, even where they admit the necessity of some measure of socialisation of any particular industry or service, to go as far as possible towards excluding all forms of political interference, and to retain as many as possible of the features of private enterprise and business management. Thus in Great Britain, the British Broadcasting Corporation and the Central Electricity Board—both statutory bodies set up for the control of services under public authority—are kept as far as possible outside parliamentary or governmental interference. Both these bodies, it should be noted, though they are definitely forms of socialisation, were established by Conservative Governments. In the case of the London Passenger Transport Act, the Labour Government's proposal that the managing board should be appointed by the Minister of Transport was altered when the Bill was taken over by the National Government into a scheme whereby the members of the board are appointed by a non-political body of trustees so as to exclude all forms of political interference. Thus the dividing line between Socialist and capitalist schemes of socialisation seems to depend mainly on the degree to which political intervention in the affairs of the socialised industries is admitted.

The illustrations given above are of course instances in which certain particular industries have been more or less completely socialised within the environment of a system under which the great mass of industries continues to be conducted under conditions of private ownership and control. In most advanced countries there has been since 1928 a considerable advance of State control over industry, and even of positive socialisation of particular industries or services. Apart from Russia, this process has gone furthest in Germany, where, even before the depression, the State had already become a partner in a large number of industrial and similar enterprises, and during the depression State participation in private industry advanced much

further, especially as the financial difficulties of the German banks, the German steel industry, and various other industries and services compelled the State to step in and provide them with fresh capital, while assuming a large share in their actual control. The German railways were indeed in form denationalised under the Dawes Plan of 1924, as the Italian railways were denationalised by Mussolini. But even denationalised railways remain necessarily under a large measure of State control, so that the change is rather in the form of operation from direct State management to management through a Public Utility Corporation than from socialisation back to private enterprise. It is even said that the British railways under the Railways Act of 1921 are already more than half nationalised—as the Bank of England and most other Central Banks are more than half nationalised—even though their ownership remains in private hands. In Great Britain even the coal industry, while remaining privately owned, has been brought under a kind of State control in the form of a compulsory cartel largely on the German model.

There is, however, a wide difference between the extension of State control in these forms, or even the complete socialisation of certain particular enterprises, and the complete change of economic system which the Socialist idea of socialisation connotes. Thus in Russia, where alone socialisation has assumed a definitely Socialist form, although all industries were not taken over at once, all basic industries passed speedily into the hands of the State, and small-scale enterprise has been progressively reduced in scope under the two Five-Year Plans, and is in process of gradual elimination. Moreover, a large beginning has been made with the socialisation of Russian agriculture, partly on a basis of actual State farming, but mainly through the institution of collective or co-operative farms, *kolkhozs*, under State control. The Russians regard this policy of socialising small-scale industry and peasant agriculture as vital to the completion of Socialism in Russia, because they hold that the Socialist attitude of mind can be developed

only under conditions of socialised economic living. The socialisation of a country is, in the view of the Russians, far more than the socialisation of its industries. It involves the radical socialisation of the entire way of life of its people.

In other countries where peasant systems are strong Socialists have been far readier, in their endeavour to secure an adequate following among the mass of the people, to promise the peasant immunity from interference with his holding. The French Socialists, for example, have repudiated all idea of bringing the land under any actual form of collective cultivation, while the German Socialists have been divided on this issue, but have regarded the collectivisation of agriculture as coming, if at all, only late in the process of Socialist evolution. Socialists, however, to whatever school of thought they belong, think at least in terms of the progressive socialisation of all major industries and services as productive agencies, and contemplate the State control of such industries as are not directly socialised through the socialisation of the processes of marketing and purchase of materials. This form of socialisation, whether it is achieved directly under State auspices or through the recognition of the Co-operative movement as an agency of socialisation, is regarded as indispensable in order to enable the Socialist State to undertake and carry through a comprehensive economic plan upon a national scale as a foundation for collective arrangements with other countries for the interchange of goods and services. Until recently, Socialist thought, except in Russia, was concentrated mainly upon the problem of socialising particular industries, with the idea of making a beginning with the socialisation of certain of the basic industries and services such as coal, electricity, and the main forms of transport. But of late two factors have combined to widen the Socialist conception of the immediate requirements of the policy of socialisation. In the first place, a growing number of capitalist industries has fallen into difficulties which seem to demand some form of collective reorganisation, and in face

of the reluctance of these industries to reorganise themselves, or of their lack of the necessary powers, there has been a growing tendency among Socialists to insist that the State ought to take them over rather than leave them after reorganisation in private hands. This applies to such industries as the iron and steel, shipbuilding, engineering, and textile trades among others. Secondly, the adoption and partially successful execution in Rusia of the first Five-Year Plan has produced a notable influence on the economic thought of Socialists and non-Socialists alike in other countries. It has induced non-Socialists to endeavour to work out schemes whereby national planning can be introduced on a basis of continued private ownership of industry, whereas it has led Socialists to think less in terms of the socialisation of certain particular industries and services and far more in terms of the assumption by an incoming Socialist Government of powers wide enough to enable it to embark simultaneously on measures of socialisation over a very wide field, and at the same time to apply drastic forms of State control to those industries which are left for the time being in private ownership. Above all, there has been a growing body of Socialist opinion which has held that the first step towards a constructive introduction of Socialism by other than revolutionary means must be the complete socialisation of the banking and financial system, including not only the Central Bank but also the deposit banks and the other leading financial agencies concerned with the provision both of short-term credit and of long-term capital for investment. This socialised control of the financial machine has been more and more regarded as the key to the entire process of socialisation in industry as a whole.

Thus we see that the word socialisation is used in many different senses, but has throughout a common core of meaning. This common core of meaning goes back to the wider sociological sense in which the word was used by the Marxists; for at the bottom of all the various plans and ideas of socialisation which have been discussed in this

essay lies the conception of a social system developing steadily towards a higher degree of integration, which brings with it a growing socialisation both of the processes of production and therewith of the services of the actual workers, manual, technical, and administrative, who attend upon the control of these processes. The socialisation of any particular industry, or indeed of industry as a whole, is thus regarded not as a thing in itself, but as the realisation in the field of economic policy of the inherent necessities of the general course of historical evolution in the modern world.

X

THE PLANNING OF INTERNATIONAL TRADE[1]

THE classical economists of the eighteenth and early nineteenth centuries rightly regarded international trade as the international form of the division of labour. Adam Smith, who began the *Wealth of Nations* with his famous chapter on the division of labour as the source of the increase of wealth in modern Societies, went on explicitly to treat of international trade as simply the extension of the same principle to cover the whole world market. Just as within each country exchange would be beneficial between one area and another, because different areas have different natural or acquired suitabilities for the production of different types of goods, so international commerce would be profitable to importer and exporter alike because of corresponding differences in national aptitudes for the various branches of production. International trade, like internal trade, was, in the view of the classical economists, essentially a process which would benefit both parties to the transaction and enable the sum-total of wealth produced over the world as a whole to be greatly increased.

Of course the classical economists combined with this view of the beneficial consequences of international commerce the strong opinion that it ought to be left utterly unplanned and uncontrolled. Intent chiefly on breaking down the barriers which had been put in the way of the free development of both internal production and exchange and international commerce under the Mercantile System, they stood for the freedom of production and trade in both the national and the international sphere, trusting to the enlightened self-interest of the individual *entrepreneur* to serve, better than any planned system possibly could serve,

[1] Originally published in *Foreign Affairs* (U.S.A.) in January 1934.

the interests of mankind as a whole. Their views, accepted by Great Britain as the basis of her Free Trade commercial policy, and echoed by later British economists, were never similarly received without question in other countries. List set up against the cosmopolitanism of Adam Smith's outlook his 'national system' of political economy; and, while some Continental economists, notably in France and Austria, went even beyond their British mentors in devotion to the principles of *laissez-faire*, in most Continental countries economists were divided, and the actual policy pursued was that of tariff protection for the domestic producer. Nevertheless, even those economists who favoured Protection in the sphere of international trade were usually strong advocates of *laissez-faire* in the sphere of domestic production; and List, equally with the Free Traders, was a strong advocate of international commerce and the international division of labour, holding that Protectionism was only the right policy for a country adapted for the development of advanced manufacturing industries, and even so was appropriate only until such a country had reached the stage, already existing in England, at which it could afford to throw down its tariff barriers and trust for its place in the world market to its productive efficiency alone. List is in fact the father of the 'infant industries' argument, and by no means of any form of economic nationalism which sets forth Protection as in the long run a sound basis for economic policy.

The Free Trade economists, however, formulated their doctrines when the economic development of the world was far less advanced than it is to-day. Within each country they thought in terms of a system of independent *entrepreneurs* competing vigorously one with another for a share in the market; and they conceived of this system as reproducing itself through the intermediacy of competing merchants in the sphere of international commerce. The first question that arises in considering the future of international trade is how far their conclusions have to be modified in the light of the enormous change which has

taken place in the actual structure of capitalist industry during the past fifty years. For nowadays within each country trusts, combines, and cartels have come to be in many industries a recognised feature of the productive system, often encouraged by the action of the State, whereas a generation ago they were ostracised or even on occasion suppressed. Nor has capitalist combination stopped short at national frontiers: a great many of the most important combines of to-day are international, in the sense that their operations extend beyond a single country, and sometimes even cover the greater part of the world market.

It is generally recognised that within any single economic system the growth of combination profoundly affects the working of the free market, by making prices no longer the result of a large number of separate bargains between individual producers and consumers, but rather the outcome of a deliberate policy pursued in the light of intelligent anticipation of demand by organisations powerful enough to control the volume of production and to set upon commodities their own prices within the limits of what consumers are prepared to pay. These limits even the most highly combined industry cannot of course escape; for whether it attempts to regulate prices or output it must in effect regulate them both in accordance with the conditions of consumers' demand. To fix a higher price for a commodity is necessarily in all normal cases to restrict sales, while to limit output is to enable a higher price to be charged. But whichever policy a combine pursues, where it is in effective operation the free market no longer exists, and the levels of prices and sales are the results of deliberate choice by the producing groups between a number of possible alternatives, and not of the uninfluenced higgling of the market. This applies even more forcibly in the sphere of international trade. For whereas there are often considerable difficulties even for strongly organised combines in the way of fixing differential prices to different buyers within the national market, combines can to a far greater extent differentiate in the prices which they charge between

one national market and another. The international combine carries furthest of all the denial of the free market and the substitution of a regulated system adjusting both supply and demand to the anticipated conditions of each particular section of the world market.

International combines, however, belong to two main types, and these two types of combine differ materially in their method of operation. The first type is that of a single centrally controlled business which is international in its sphere of operations, and sometimes but not always in the essential composition of its controlling body as well. But in practice combines of this kind tend to be far less international, in any cosmopolitan sense of the term, than imperialistic. They tend, like the great oil trusts, to radiate outwards from one of the great industrial countries, establishing subsidiaries and connections in other countries without losing the essentially nationalistic or imperialistic character of their controlling agency. Thus in cases of this type it is common to find one great international combine, closely associated with one great country, in keen competition with a second combine no less closely associated with another country, or perhaps with several others of the same type. Combines of this sort may come to agreements one with another limiting the forms of competition in which they will engage, or even sharing out particular markets; but they remain essentially competing bodies, aiming at expanding their sales one against another, and also commonly in sharp rivalry for the control of new sources of raw material supply.

The second type of international combine, best typified by the Continental Steel Cartel, is on the surface far more international than the great imperialist trusts. But combines of this second type, while their composition and control are international, are commonly made up of national units, each of which retains its independence within the wider body. They are, moreover, usually terminable cartels and not fully organised financial unities, and it is quite possible for them to fall asunder on account of a quarrel

between the national groups of which they are made up. They are, indeed, less bodies for the establishment of industry upon a cosmopolitan basis than economic treaty-making bodies, which aim at the regulation and limitation of competition, on terms, between rival national groups.

It is important to realise that, in spite of all that has been said about the progressive internationalisation of modern business methods, neither of these types of combine really makes for internationalism in any sense calculated to remove or diminish the effect of rivalries between national economic groups. It is not really true that Capitalism is tending to become more international in any sense in which internationalism implies the diminution of the strength of nationalist forces. Indeed, the very opposite is the case; for the tendency is all towards the closer linking up of nationally or imperially organised producing and trading units with the Governments of the States with which they are chiefly connected. Economic Nationalism has often been written about in the post-war world as if it were a special vice of the newly created small post-war States; but in fact it goes far deeper than this, and is intimately connected with the imperialist phase upon which capitalist civilisation has decisively entered during the past fifty years. The Economic Nationalism which exists in the smaller States is, indeed, the more disastrous in its effects upon wealth in that a small State is necessarily ill-equipped for developing within its borders a wide range of industries in such a way as to take advantage of the economies of large-scale production. Economic Nationalism in a small State impoverishes the people of that State; but Economic Nationalism writ large as imperialism in the policies of the great States, while it is directly destructive of the opportunities for wealth-making only in a less degree, may be far more disastrous if it is the cause of imperialist world wars.

In a world organised economically and politically as is the world of to-day, there is plainly no prospect at all of a reversion to the freedom of international commerce, in the sense in which it was advocated by Adam Smith and his

successors of the classical school. Arm-chair economists may continue to dream of the superior advantages of a Free Trade world, but there is no more chance of their dreams coming true than there is that Europe will return to the localised economic system of the Middle Ages. The old Free Trade era has definitely gone, and can never be restored.

Nor can we reasonably wish for its restoration. For the old Free Trade case in international commerce rested on the assumption that domestic trade and production would be left to the higgling of the market between individual consumers and individual competing *entrepreneurs*. But in these days every country recognises within its own national economy the need for a large measure of planned control. Even the most capitalistically minded countries have moved with enormous rapidity in this direction during the past few years. Germany, the pioneer in this field, was the first to turn from the discouragement to the positive encouragement of national forms of combination; and other countries, more permeated by the Free Trade tradition, were only slower to realise that their national capitalist systems were speedily passing out of the phase of competition into one of growingly close national combination. Nowadays 'trust-busting' is an obsolete sport, and even the United States, under its National Recovery Act, has suddenly reversed its entire policy, and turned from an insistence on domestic *laissez-faire* to a highly developed system of national industrial regulation.

At present, when countries turn from *laissez-faire* ideas to the attempt to regulate their national industrial systems, they commonly do this in the first instance largely by means of tariffs or analogous forms of control over imports. Tariffs are increasingly supplemented by quotas, prohibitions, and systems of importation only under licence; but the common feature among all these policies is that they are endeavouring to guide and regulate national production chiefly by imposing restrictive measures on international trade.

Why does this happen far more readily than the direct regulation of the internal productive system? The answer is that it happens mainly because tariffs and, to a less extent, the various forms of non-tariff protection are known and familiar devices, which can be used not only without creating an outcry from the property-owning classes, but with the support of large sections among them; whereas any attempt directly to control production is at once met with the cry of 'bureaucracy', and often with the allegation that such plans are in their essence 'socialistic' and therefore fatal to the rights of property. This is exceedingly unfortunate, for it means that where the recognised need for national planning impinges on international trade, it does so practically always in a restrictive fashion, and hardly ever so as to encourage desirable forms of international exchange. Yet clearly if there is to be national planning, there ought to be international planning as well, and international planning ought to take the form not mainly of restricting the movement of goods from one country to another, but rather of encouraging large-scale bargains for the exchange of goods wherever these are of such a nature as to be of benefit to both parties to the transaction.

For, although to some extent the scope of international trade may be lastingly lessened by the rise in all the more advanced countries of much the same range of industries, and although the later developments of industrial technique have been such as largely to offset the national suitabilities of particular areas for the carrying on of particular branches of production, there remains an enormous sphere within which national specialisation is still desirable, and indeed absolutely necessary if full advantage is to be taken of the economies of large-scale specialisation and standardisation of output. Probably international trade will not, in the twentieth century, bulk so largely in the total economy of any country as it bulked during the past century in that of the most developed industrial States, or in those agricultural States which had concentrated on

specialised production for the markets of the industrial countries. But even if this is true, the scope that remains open for organised exchange between planned national economic systems is very large, and it will be a disaster for the world if the problem of international trade is regarded in the name of Economic Nationalism mainly from a restrictive standpoint.

It is, however, bound to be so regarded until countries deliberately and consciously take direct control of the volume and direction of national production. For as long as national production is left unregulated, or is regulated only indirectly by means of tariffs and similar devices, there is no possibility of economic collaboration between States in any form which is not principally restrictive in its effects. One country can of course agree to give tariff preference to another; or some form of customs union may be built up between neighbouring States—though this is for the moment to a great extent obstructed by the Most Favoured Nation Clause, which appears in so many commercial treaties. There can be 'Ottawa' Agreements and, if the Most Favoured Nation Clause is modified by agreement, 'Ouchy' Conventions, among States. But States cannot, save in very exceptional cases, come under present conditions to agreements designed positively to encourage trade between them except by taking measures definitely designed to exclude trade with some other country. Restrictive collaboration is possible, and does occur: direct planning for an increased volume of international trade is practically excluded under present conditions.

The prerequisite of constructive international planning is, we have said, national planning. If a State is to place itself in a position to make bargains with other countries for the definite admission of certain quantities of their goods, it must do this with full knowledge of the amount of these goods which it aims at producing within its own frontiers. It must therefore have a national plan of production under which the available resources of materials, machinery, and man-power are definitely assigned to

different branches of production, as they are under the planning system of the Soviet Union. Armed with such a plan, a country knows what it needs to import and is in a position to make constructive bargains with other countries for procuring these necessary imports in exchange for those commodities of which it is able to produce a surplus for export. It can modify its own production plan so as to fit in with bargains into which it enters with other countries, deciding to limit its activities in one industry so as to expand its production in some other sphere, or perhaps to give up producing certain types of goods altogether in order to buy them from a country better able, with the aid of its market, to make use of the full economies of large-scale production. Such a country can make a plan for the full utilisation of its own productive resources in such a way as to fit in this plan with the largest volume of international exchange which national differences of productive efficiency make desirable and other countries can be induced to agree to. At present Russia is the only country which is in a position to make with full knowledge bargains of this sort; and Russia cannot in fact make them, because there is no other country similarly equipped with which they can be made. But if the world is to advance at all effectively in the direction of a planned economy, it is only on this condition that the advance can be made. States, or national economic organisations acting with the full authority of the State, must be in a position to make collective bargains one with another in the light of a full knowledge of the use which is to be made of the national productive resources in accordance with an organised and approved national plan.

Any fully developed system of international planning thus demands not only national planning as its first prerequisite, but also unified control over its foreign trade. Where these two conditions are satisfied, tariffs and similar forms of Protection, unless they are preserved merely for revenue purposes, become obviously irrelevant. For the tariff, like the other forms of Protection now in vogue, is

essentially an instrument for influencing forms of international trade which are not under the direct regulation and authority of the State. There can be no need on Protectionist grounds for a State, or a national economic authority acting with the State's support, to have tariffs on the goods which are brought in under its own authority. The extraordinarily uncertain and two-edged weapon of the tariff can be replaced by the absolutely certain instrument of the direct control of buying as a method of regulating the quantity of goods imported from abroad. Moreover, the controlling authority will be in a position not merely to limit or increase from day to day the quantities of foreign goods of any particular type that are allowed to cross the frontier, but also to make well ahead bulk contracts for the delivery of imports which are certain to be required on account of the nature of the allocation of domestic productive resources under the national plan.

Of course if national planning does come to be the basis of the economic activities of a number of advanced States, it is not likely to arise in them all at once unless it comes as the consequence of a convulsion similar to that which tore up the roots of the old Russia in 1917. Whether national planning comes elsewhere as a consequence of a constitutional Socialist victory or as an instrument devised for the restoration of prosperity in a country still under capitalist control, it is likely to be introduced by stages, and to be applied in the sphere of foreign trade, not simultaneously to all industries, but gradually, starting with those industries which are most important in international exchange and most easily susceptible to methods of bulk control. Broadly, from the standpoint of international planning, the goods which pass in international exchange can be classified in three groups. The first group consists of those foodstuffs, raw materials, and standardised semi-manufactures which are readily capable of quantitative and qualitative measurement, and therefore lend themselves fairly easily to processes of collective

bargaining leading up to bulk contracts of sale. At the other extreme stand those finished commodities which are produced in relatively small quantities, or even individually, for the satisfaction of particular and limited demands. This second class of goods includes not only the more diversified types of consumption products, but also a high proportion of capital goods, and it is therefore of great importance in the exchange economy of the more highly developed countries. Between these two extreme types of product stands a third group, consisting of those manufactured commodities which, while they are produced under large-scale conditions, are widely diversified in quality and fashion, and therefore less easily regulated than the commodities belonging to the first type. Wheat and coal may be taken as outstanding examples in Group 1, ships and machinery and many luxury products as typical examples of Group 2, and most textile goods, boots and shoes, and other consumers' bulk lines as typical of Group 3.

When international regulation is taken in hand, each country will be disposed, where it can, to begin by planning the production and exchange of the commodities which fall within Group 1; for this will be by far the least difficult part of the problem. Where countries can arrange for the bulk exchange between them of commodities falling within this group, it will be easiest to arrive at a system of internationally planned exchange. It will not, however, be possible to advance very far by this method alone, as to a great extent world trade consists not of the exchange of Group 1 products for Group 1 products, but rather of the exchange of Group 1 products for products falling within Groups 2 and 3. If, therefore, the exchange of goods between planned economics is to be advanced far, there will have to be arrangements for the organised buying and selling of products falling within the latter groups as well. The tendency will doubtless be in this case to concentrate first of all on Group 3 products rather than on Group 2, because the products in Group 3 are also to a large extent

standardised and can therefore be made the subject matter of bulk systems of exchange. But there will arise also a special question relating to one important element falling within Group 2. For some countries which are in a position to export chiefly Group 1 products will desire to receive in exchange to a great extent capital goods. This, for example, is bound to be the position if the U.S.A. and the U.S.S.R. enter, after recognition, into any large-scale agreement for mutual trading.

The problem of organised international exchange, taken as a whole, has two main aspects, that of arranging for the exchange of goods, and that of arranging for the necessary payments across the national frontiers. To the extent to which bulk contracts can be arranged on a bilateral basis, at prices agreed in advance, the need for monetary payment across national frontiers can be made to disappear by a system of crediting the value of the goods exchanged to the account of the seller in the currency of the buyer, and then using the money to pay for the goods exported under the corresponding bulk contract involving a reverse movement of goods. But where the exchange is not of bulk products under Group 1, or perhaps Group 3, but involves Group 2 products to any considerable extent, the financial part of the exchange will assume far greater importance, though it will have to be dealt with along the same lines. In this case the country selling bulk products in exchange for a more diversified range of Group 2 products will be able to know in advance how much of the currency of the purchasing country its exports will command; for it will be possible in the case of the bulk exports to fix the price in advance. But it will not be possible to have similar foreknowledge of the exact quantity of Group 2 goods that this supply of currency can be used to acquire. Accordingly there will have to be a system of running credits for each country in the banks of the other country, worked in such a way as to stabilise as far as possible the exchange rates between the two currencies, though not necessarily to fix them against the operation of major forces. This implies close collabora-

tion between the banking systems of the countries organising the exchange as well as between their national trading organisations.

This whole problem is of course highly technical, and cannot be fully worked out until the nature of the proposed exchanges of goods has already been determined, at any rate approximately. It is, moreover, bound up with the question whether the exchange of products between the two countries is to be an exchange that balances in terms of commodity trade, or is to include a large or smaller export of capital from the one country to the other. Obviously the entire question of international lending for industrial purposes is closely bound up with the organisation and planning of international trade; and countries entering into mutual trading agreements on a collective basis will have to include in these agreements any arrangements which they desire to make for the movement of capital from the one country to the other, since the failure to take account of this factor would speedily upset the financial aspects of their trading relationship. This means that international equally with national planning involves the control of capital investment. A country cannot have a national economic plan unless it is in a position to guide the investment of capital into those industries in which the plan requires the provision of additional capital resources, and to prevent the dissipation of investments in services not scheduled for development under the plan. Similarly, if a system of organised international exchange is to be worked out, the planning of the export and import of capital obviously forms an essential element which will have to be controlled in its proper relationship to the organised movement of commodities.

What are the chief obstacles at present in the way of the development of an organised system of national planning such as I have endeavoured to foreshadow? First and most obviously, the absence in all countries except Russia of any real approach to a planned national economy; for, as we have seen, in the absence of this the relationships between

countries in the economic sphere are bound to be mainly restrictive, and to aim rather at preventing than at developing international trade. What, then, are the obstacles to the development of national planning? First and most obviously, the individualism of business *entrepreneurs*, and their continued belief in the merits of a system which gives each possessor of productive assets the maximum opportunity for the display of his individual 'enterprise'. This individualist tradition is powerful in the minds of the business *entrepreneurs* in most of the more developed countries, and especially in the older industries of Great Britain, among the relatively small-scale industrialists of France, and almost everywhere in the United States. It is far less powerful in Germany, or indeed in any of those countries which have developed industrialisation at a fairly late stage, and have thus entered upon large-scale production under conditions already dominated to a large extent by the growth of trusts and combines. But powerful as this individualist tradition is in the older industrial countries, it is being rapidly broken down by sheer force of economic circumstances; and it is safe to predict that whether the world economic system is reconstructed mainly under Socialist or under capitalist auspices, some considerable advance away from individualism and towards a planned economy is certain to be made. What is doubtful is whether a planned economy introduced under capitalist conditions can possibly so establish itself in face of the powerful vested interests with which it will have to deal as to exercise the degree of control over the use of national resources necessary to afford a sure foundation for a system of internally planned production and trade.

The danger is that, if a planned economy is introduced under Capitalism, it will become the prey of powerful vested interests, which will thwart the intention of promoting a distribution of the national man-power in the interests of the maximum welfare, and, instead of aiming at the conclusion with other national groups of agreements designed to encourage international exchange, will resume

the imperialist policies characteristic of the later stages of capitalist development, and press these policies with the added strength derived from the closer relationship between the State and the economic order which national planning necessarily involves. If this happens, national planning, so far from serving as a force for the liberation of international exchange and the increase of world production, may easily turn into an instrument for the drastic restriction of both. For it may aim at maintaining in the home market a policy of high prices by the restriction both of domestic output and of permitted imports, and at the same time seek to expand its sales in the world market in order to offset the limitation of domestic demand, which such a policy of high prices inevitably connotes. Under such conditions national planning will lead not to the regime of plenty which is now well within the world's grasp in view of its greatly expanded productive power, but to a perpetuation of scarcity, and to the shutting up of each developed country more and more behind a wall of Economic Nationalism, save to the extent to which the stronger countries are able by the methods of economic imperialism to force their way into the markets of the weaker and reduce the smaller countries to the position of satellites.

There was ample evidence at the World Economic Conference that many of the world's statesmen and leading business men, when their thoughts turned in the direction of planned national and international trade, considered this far more as a means of restricting output and so raising prices by the creation of artificial scarcity than as an instrument to be used for increasing the world's total wealth and prosperity. Fortunately in most cases these plans for the perpetuation of scarcity came to nothing in face of national jealousies and rivalries too powerful to be overcome—for it is possible to applaud the result even while one deplores the reason. The World Economic Conference was in fact a powerful object lesson in the existing force of national and imperial economic hostilities, and in

the immense accession of strength which the *sauve qui peut* of the present crisis has given to the forces of Economic Nationalism. National planning in itself affords no way of escape from this regime of national isolation. It is an instrument which, like most instruments, can be used for good or ill according to the character and motives of the forces which control its operation. But national planning on a good or on a bad basis is bound to come; and it is for those who believe in international solidarity and in the international division of labour as means of increasing the world's wealth to use all their efforts to ensure that, when it does come, it shall come under the right auspices. This involves that it shall be controlled by those who mean to use it, not for the purpose of bottling up each nation within its own frontiers in a mistaken belief that it is somehow possible to sell more than one buys, and to take advantage of the economies of large-scale production within a nationally restricted market, but instead for the liberation of the vast productive energy which is now lying unused all over the world by creating a system of organised international exchange on a basis of mutual advantage and superseding tariffs and other restrictive devices by large-scale arrangements for the collective interchange of complementary products.

XI

INHERITANCE [1]

INHERITANCE, the entry of living persons into the possession of dead persons' property, exists in some form wherever the institution of private property is recognised as the basis of the social and economic system. But the actual forms of inheritance, and the laws and customs governing it, differ very greatly from country to country and from time to time. There is no 'natural' law or principle of inheritance, which is essentially a changing thing, based on the changing forms of economic and social organisation. For the special laws and customs governing inheritance are always and everywhere part and parcel of the general structure of property relationships. Changed ways of owning and using property will always bring with them, in the long run, alterations in the laws and practices relating to the inheritance of wealth.

Unless there is private property, owned or possessed by individuals, a problem in connection with the question of inheritance hardly arises. For whereas an individual dies, and his property, if he has any, has to be disposed of in one way or another, a group, such as a class, or tribe, or family, does not die. Members of it die, and are replaced by new members in the common enjoyment of the property of the group. But the property itself never changes hands, or needs to be disposed of. There is no inheritance, in the sense in which the word is used in this essay, because the group, which goes on, and not the individual who dies, is conceived of as the repository of the right of possession. This is one reason why inheritance plays a very small conscious part in the life, or in the laws, of most primitive

[1] Based on an article published in the *Encyclopaedia of the Social Sciences.*

Societies. Individual ownership either does not exist among them, or is confined within a very narrow range. The group holds in common, and is tenacious of its rights. The individual does not hold, but only shares in the use; and accordingly, when he dies, there is nothing for anyone else to inherit.

Even where there is individual property of a sort in primitive Societies it can seldom be inherited. For where most property is group property, what is recognised as a man's own is usually limited to things so personal to himself that it would appear impious to hand them over to another at his death. His weapons, his simple tools and utensils, are thought of as extensions of his own personality, as in modern times Hegel and other philosophers have thought of property over a far wider field. As part of his personality, they are often to be burned or buried with him; and this tendency is the stronger because it is commonly believed that the dead will have need of them in another world, where he will be still a warrior, or a smith, or a tiller of the soil, rather than a merely undistinguished angel with wings and a harp. He must take his means of creation and expression of his personality with him to the other world, and consequently no one else may inherit them in this. The very idea of inheritance in any shape or form is slow to develop in Societies where private property is only in a few things of personal use, and in most things group possession is the rule.

But as fast as private property develops, and especially as soon as it touches the means of production beyond mere tools of a craftsman's trade, inheritance comes with it. Indeed, property in the sense of ownership is not essential. It is enough that there should be private possession and use. For rights over things can be passed from the dead to the living as well as things themselves. There is a right to succeed to a tenancy as well as to the ownership of a farm; and many forms of inheritance are in effect successions to rights—and sometimes to duties—rather than to things. This is obviously true of hereditary titles and

offices, as well as of many forms of feudal and similar tenure. Indeed, in one sense all inheritance is of rights or duties; and these rights and duties are only sometimes embodied in material things.

The inheritance laws and customs of Societies are apt to be most complicated where they are still based, in part at least, on a lingering sense of group possession or ownership. Complete freedom to bequeath property, or to give it away during a man's lifetime, can only develop under social and economic conditions based on highly individualistic notions about ownership. A thing must be absolutely a man's own, in a most individual sense, for him to have a full right to give or bequeath it to whom he wills. Indeed, only among English-speaking peoples, and by no means completely among them, does full freedom of bequest exist to-day, or has it ever existed; and even in their case it is fairly modern—a product of a growingly individualistic economic system. It does not exist in Scotland even now, or wholly in the United States; and there is no continental country in Europe that even approaches it. Everywhere, except in England and in countries which have borrowed their legal institutions largely from England, property still retains something of a group character. It is not purely personal; and it has functions apart from the purposes of its possessor for the time.

This is most clearly seen in such institutions as the *legitim*—the legally enforceable claim of widows and children to at least a part of a dead husband's or father's estate. The *legitim* takes many different forms; but it exists in some form and degree in the great majority of countries. It existed, for example, in Ancient Rome, where the law of inheritance seems to have begun by admitting without question the right of the children to succeed to the father's estate, and only gradually to have admitted a limited freedom of testamentary disposition. Nor is it reasonable to regard this system simply as a restriction on the right of bequest; for that would imply free disposal of property by will or gift to be the natural and obvious thing. But in fact

it is so far from being natural or obvious that it has never entered into the heads of the great majority of mankind that it ought to be the main way of disposing of property on the death of its possessor. On the contrary, in all peasant countries there is still a strong tendency to think of real property at least as belonging to the family rather than the individual. It is the family's means of life, from which no member can be shut out except for positive misconduct. Property is no longer common to the family, as it used to be to the clan or tribe; but neither is it purely the personal possession of the head of the family.

Naturally, this notion of a group right or claim clings most tenaciously to forms of property which the group actually uses as instruments of production; for in these cases the danger of lessening its productive value by comminution is great. The more property ceases to have this character, or takes the form of money or shares in undertakings which are not purely family affairs, the less the group feeling remains attached to it. The family's claim to money, or to shares in a joint stock concern, is far less deeply rooted in tradition, and seems far less compelling, than its claim upon the family estate as a means of life. Townsmen in India often exist wholly or in part on pittances derived from the family land, which is regarded as charged with the maintenance of all its members. But even where property takes a money form, or that of paper claims on the earnings of businesses outside the family's control, the notion of the estate as a group possession usually dies hard. It is not dead even in England or the United States; for even there it asserts itself, not only in the laws governing intestacy, but also even more powerfully in social custom, influencing the wills men actually make, even when they have full legal freedom to make what wills they like.

Modern forms of economic organisation are very powerful solvents of the group notion of property; for they tend to make the claims to income arising out of property divisible without the need for dividing the property itself.

The chief argument against the *legitim* in most of its forms is that it tends to a more and more minute subdivision of property. Where landed property is the chief form of wealth, this may have very serious results, not only in the breaking up of large estates, but also in the subdivision of peasant holdings to a point which makes agricultural improvements impossible, and reduces holdings to a size too small to admit of a tolerable standard of life. The institution of primogeniture has been upheld mainly on the ground that it keeps estates and agricultural holdings together, and thereby makes it possible to develop them more efficiently for the production of wealth. When, however, property comes to consist largely of stocks and shares, the arguments against division have far less force. In public companies and corporations, the parcelling out of the shares among a larger number of holders has no effect at all on the management; and even in the case of family businesses charges can be made on the net earnings for different members of the family, and where such a business is turned, as now often occurs, into a private company, actual shares can be issued, and the business still carried on without change of policy. It can be urged that the setting up of charges on the business, or the diffusion of the ownership of shares, makes the accumulation of capital out of reserved profits harder than it would be if the whole business were inherited by a single owner. But this is only one aspect of the wider argument that great inequalities of wealth and income are necessary for the adequate accumulation of capital in modern Societies. In general, there is no doubt at all that the institution of shareholding in joint stock concerns as the outstanding form of property-ownership has made far easier, and less open to economic objection, the diffusion of estates at their owners' death.

This diffusion tends to a more individualistic conception of property rights; for, save in the special case of businesses which retain their family character, the divided property loses all unity, and becomes simply part of the separate estates of the various inheritors. It may still be regarded

as the duty of the richer members of the family to help maintain the poorer; but this becomes a purely social duty, unconnected with the conception of a family estate charged with the maintenance of all the members. Only in the case of landed estates does this notion retain any force in developed industrial Societies; and even in that case it has been greatly undermined. In peasant Societies, on the other hand, the idea of the family holding as charged with the family maintenance still retains great force. Often most of the family are driven or impelled to go away and work elsewhere—as factory hands or labourers, or, in a higher stratum of society, as doctors or civil servants or lawyers. But even when they have left the family property, the notion of its responsibility for helping them in adversity survives with almost undiminished force.

We are here concerned, however, chiefly with the working of the institution of inheritance in modern industrialised Societies, where the conception of property has become highly individual, and the family survives as a social rather than as an economic institution. In such Societies, as we saw, the tendency has been to leave inheritance as free as possible from regulation by the State, and therefore to extend more and more the right of unfettered bequest. The State has still to lay down what is to happen in cases of intestacy; but with the growth of the will-making habit, fostered both by the growth of education and by the enlarged freedom of bequest, intestacy becomes of less importance in practice. Most people with anything considerable to leave do dispose of their property by will; and they are left a very wide discretion—in most English-speaking countries practically complete freedom—in doing this.

In the early nineteenth century, in England at any rate, freedom of bequest came to be widely regarded as an integral part of *laissez-faire*. The classical economists, especially McCulloch, argued strongly against the *legitim* and in favour of primogeniture as a social institution, on the double ground that division of property made against efficient production and that the disinheriting of younger

children gave them the maximum incentive to make their own way in the world. A secure competence they regarded as disastrous, both for Society and for the individual who enjoyed it; and they urged that men would be spurred on to make the best use of their powers only by need and by emulation of the rich. Inequality was defended as a means to the accumulation of capital, and primogeniture favoured on the ground that, though it might be bad for the heir, by making him lazy, it was good for the younger children and the community. According to McCulloch it was a positive privilege to be disinherited; but it did not enter into his head that the best thing would be to disinherit everybody.

But while primogeniture was favoured, there was no desire to enforce it by law; for freedom of disposition by will was regarded as a necessary incentive to the accumulation of capital, and it was intended that the father should be able to leave his property away from his children, and thus have the whip-hand of them while he lived, and the authority to induce in them virtuous and industrious habits. The object was to give men the greatest possible incentive not only to make, but also to save, money; and this would be best secured by putting what they made and saved absolutely at their free disposal. Despite Jeremy Bentham's pleas for limitation of inheritance through taxation, the nineteenth-century doctrine of property and inheritance developed in England on purely individualistic lines, in strict keeping with the philosophy of *laissez-faire*. In this field, as in many others, it was left for John Stuart Mill to go back on the classical tradition, and to propose, in addition to some restriction on the right of bequest, a severe limitation of the sum which any one individual would be allowed to inherit from any source. Mill is hesitant; for he is impressed with the undesirability of doing anything to check capital accumulation. But he also dislikes, and desires to reduce, inequality; and his work is at several points the forerunner of modern doctrines dealing with taxes on inheritance.

Before Mill, the question of inheritance was considered,

except by the Socialists, almost solely in relation to the accumulation of capital and the efficient use of productive resources, and hardly at all as a problem of social justice. In Mill the two points of view are in conflict; and from his time the question has always to be considered from both standpoints. On the one hand, inheritance and freedom of bequest are defended as necessary incentives to saving, and as means to the more effective use of capital; for, given freedom of bequest, it is held that men will tend to leave their capital in such ways as to promote its effective use. On the other hand, inheritance is attacked as one of the greatest sources of social and economic inequality, and proposals are made to limit or even to abolish it in order to secure a better distribution of incomes.

Abolition of inheritance, however, can hardly be urged as a self-contained and sufficient reform. For if property is to lapse to the State at its owner's death—and that is what abolition involves—the State will have either to make use of it for production under collective control, or to let it out to the individuals who seem best qualified to use it. The former is the Socialist solution: the latter has been urged by various small groups from time to time, and is urged to-day by the followers of Rudolf Steiner. In either case, the abolition of inheritance involves a radical change in the economic as well as the social system, and especially new methods both of accumulating and of using capital. It would also involve, at any rate in the first generation, some restriction on gifts *inter viros*, such as a real enforcement of the *legitim* also demands; but whether such restriction would remain necessary after the first generation would depend on the opportunities for fresh capital accumulation still left to the individual. A thorough Socialist system, such as exists in Russia now, does not need this; for it affords hardly any opportunity for fresh accumulation, and the State has ample means of dealing with such accumulations as do arise. Russia in 1918 abolished inheritance completely, with only provision for meeting claims from relatives based on proved need. All property in Russia was to

pass to the State at the owner's death; and that, in view of the narrow opportunities for acquiring fresh wealth, appeared to settle the problem. But, as we shall see later, Russia has since modified this drastic legislation. There is inheritance in Russia to-day; but it is confined within very narrow limits.

There can be no doubt that under any Socialist system, even if it fell far short of Communist thoroughness, the right of inheritance would be, in practice, very severely restricted. For with the instruments of production in the hands of the State, the chief means of private accumulation would be gone, and therewith also the need for it. The accumulation of capital would clearly become, under such a system, a collective function of Society, and no longer a matter for the individual. Incomes would be distributed after subtracting the amounts needed for the provision of new capital equipment; and they would be meant for spending and not for saving. Inheritance would thus come to be restricted at most to things of use, and could not include instruments of production, except during a period of transition. Probably, even within these limits, it would be further restricted by law, at any rate as long as any considerable inequalities of income remained in being. For, with the development of social services, the argument that a man needs to provide for his children would be progressively undermined. Probably the bequest of personal possessions up to a limited amount would be allowed; but inheritance in excess of this would be likely to disappear, not so much because it would have been deliberately stamped out, though this might be the case, as because the need and opportunity for it would alike have gone. It would have lost both its economic and its social functions.

There has been a good deal of dispute among economists about the extent to which the inheritance of wealth is in modern societies the principal cause of inequality. Undoubtedly, its influence is likely to be greater in older settled countries than in new countries still largely at a pioneering stage. For the older countries have already

much larger masses of inherited wealth, and usually greater opportunities for investing it securely so as to perpetuate its existence. The familiar parable of 'clogs to clogs' in three generations belongs not to the old and settled but to the new and adventurous type of industrialism. Invested money, from which the owner simply draws a revenue without venturing it in risky undertakings, is in old settled countries largely self-perpetuating. There are losses, of course; and men do sink from class to class on occasion. But under ordinary conditions, in such countries, reasonable prudence secures the perpetuation of wealth once acquired.

There are also, in old countries, usually fewer opportunities for the rapid acquisition of wealth by those who start life without it. There are some, no doubt; and there are plenty of chances for the rich to become richer. But the older and the more settled in its economic habits a country is, the more likely wealth is to go to those who have some already, and the smaller proportion of men are likely to rise from nothing to great fortunes. Unless he has very exceptional business qualities, the able man who starts with nothing is more likely to end up with a good salary than with a large fortune.

There can, then, be no doubt that in the older settled Societies, inheritance is a very big factor indeed in causing economic inequality, though it is to be wished that the whole question should be more fully investigated than it has been as yet. It counts for a great deal, not only in perpetuating large fortunes, but also in giving those who inherit even quite small fortunes a very long economic start over those who do not.

In the newer countries, the influence of inheritance is probably less decisive, both because the current accumulation of new capital bears a higher proportion to the amount of inherited wealth, and because, conditions being less settled, there are more opportunities for a man to rise, either by accumulating capital for himself out of profits, or by getting put at the head of a big business on the score

of ability alone. Such countries, however, as they grow in wealth, rapidly accumulate heritable property, and begin to develop a propertied class distinct in some degree from the class of successful business men. The United States has already a large class of this type, though inherited wealth still probably counts for relatively less in America than in either Great Britain or France.

In nearly all countries, the proportion of those dying who have anything substantial to leave is very small indeed. In Great Britain, according to estimates made by Professor Henry Clay, before the war only 15 per cent of all persons possessing incomes of their own had a total capital wealth of over £100, and only $6\frac{1}{2}$ per cent had more than £500. Even in 1920–1921, when prices were very high, only 25 per cent had over £100, and less than 12 per cent over £500. In Prussia, according to Dr. King, only 14 per cent had over 6000 marks in 1908.

Inheritance, in any economically significant form, is thus confined to a comparatively small section of the population. Nor can there be any doubt that in the main those who die leave most of their money to persons of the same social class as themselves. There are, of course, many small legacies to poor relations, servants, and employees; but apart from charitable bequests, the bulk of property tends to pass to relatives occupying a similar social status to those from whom they inherit. This causes inheritance, even on a basis of freedom of bequest, to act as a powerful force in perpetuating inequalities in the distribution of wealth and income. Gifts and bequests to charities have, indeed, an opposite tendency; for they usually result in the distribution of increased incomes or services to the poorer sections of the population. But in no country—not even in the United States—is the amount of gifts and bequests for education and charity large enough seriously to affect the distribution of wealth in Society as a whole.

The inheritance of wealth lies, then, at the very roots of the class-structure of modern communities. It is not suggested that class-divisions would disappear if it were

abolished; for if the change stood alone differences of wealth and income arising within the lifetime of the individual would still be enough to lead to wide differences in education and in equipment for money-making. The rich parent could still give his children a preferential start in life by expensive professional training, or by setting them up in business for themselves. It is, however, as we have seen, inconceivable that the abolition of inheritance should stand alone. If it came about, it would certainly be accompanied by increased public provision for higher education, which would undermine class-monopolies in the professions, and by a restriction of opportunities for the application of private capital to business enterprise. Inheritance is by no means the only source of class-divisions and great economic inequalities; but it is difficult to imagine their persistence without it in anything like their present form. This is the case, however, primarily because of the other social changes which the abolition of inheritance connotes, and only secondarily because of the direct effects of abolishing it.

Short of abolition, the rights of bequest and inheritance could, of course, be drastically restricted, without the immediate necessity for any complete change of economic system. Mill's proposal to limit the amount that can be inherited, instead of the amount that can be bequeathed, has been nowhere acted upon; but one State after another has introduced some form of inheritance taxation, and thus confiscated to the public purse some part of the fortunes of those who die with any considerable property. Such taxation has many forms in different countries; but it usually involves some degree of graduation according to the total value of the estate, and also some discrimination according as the property is left to nearer or remoter relatives, or to strangers. In Great Britain, where the sums raised in this way are now considerable, and bear heavily upon the larger estates, the taxation is graduated mainly according to the total value, and only to a less extent according to the relation of the beneficiary to the

testator. It is, in fact, chiefly a method of taxing big accumulations of wealth, and not of influencing freedom of bequest. In 1929–1930 Death Duties in Great Britain yielded a net revenue of nearly £80,000,000, as compared with nearly £295,000,000 from direct taxes on incomes. But this sum, large as it is, is not nearly considerable enough to have noticeable effects in reducing inequalities of wealth or income.

It is sometimes suggested that this failure to reduce inequality by taxation of inheritance is in itself a sign that most big fortunes are made rather than inherited, and that inheritance is not so powerful a factor as has been supposed in causing inequality of income. But this is to ignore the great power which large fortunes have to attract more money. If it were not for Death Duties, the distribution of income in Great Britain would be still more unequal than it actually is. What is left of such fortunes after taxation is amply enough to serve as a preferential basis for the accumulation of further wealth. It is not denied that in Great Britain, unlike the United States, economic inequality has been somewhat diminished of late years; but this is a result far more of the heavier taxes on incomes than of the taxation of inheritance.

It is, in effect, impossible to divide the wealth of the richer classes into two parts, the one inherited or the result of gifts *inter vivos* which are really a form of inheritance, and the other acquired by the owners' personal exertions. For this is to ignore the truth that money breeds money, and that it is far easier for a man who inherits money both to make more and to save out of his income than it is for one who starts with nothing. Fresh capital accumulations are in part the result of saving out of inherited fortunes; and the invested capital on which large profits are made is in part inherited money. What a man makes in his own lifetime may be fully as much a result of his inheritance as of his personal skill, luck, or exertions. It is therefore a sheer impossibility to isolate in any quantitative sense the results of inheritance. But

it is fully possible to say that incomes and property would be very differently distributed if everyone started with an equal supply of capital.

But, however great the social and economic influence of inheritance may be admitted to be, it will not lack defenders as long as it is considered to be a necessary condition of the accumulation of capital. It is true that the growing tendency for industries to finance their own expansion out of reserved profits has led to some substitution of group for individual saving, and thus to a considerable extent lessened the need for private accumulation out of incomes; and it may be that this group method of saving foreshadows a time when industry will be wholly self-financed, or at any rate when the calls for capital out of individual savings will be much reduced. But for the present individual investment continues to play a substantial part in financing production; and it is therefore deemed necessary to keep up the rate of saving, though some economists, notably Mr. J. A. Hobson, have suggested—I think rightly—that in prosperous times capitalist Societies attempt to save and invest too large a proportion of their incomes, with the result of causing a deficiency in the demand for consumers' goods. There is much to be said for this view, which would provide an economic justification for measures tending to reduce the volume of saving in prosperous times—including the higher taxation of inheritance at such times, and the appropriation of the proceeds as revenue and not as capital. But it cannot be held that this tendency to over-saving exists, in the same degree at any rate, when times are bad; while it is precisely at such times that the State, hard pressed for revenue, is likeliest to use capital taxes for meeting current expenditure.

In any case, the need for private accumulation of capital does still exist in a considerable degree in modern capitalist Societies; and inheritance will continue to find defenders on the ground that it does promote this end. It will indeed be defended not so much in spite of its tendency to

aggravate inequalities of wealth and income, as because of this tendency. For there is a school of economists that maintains that the richer the rich are, the richer will the poor be also, because the highest production and the highest wages will be secured when profits are highest, and profits will tend to be highest in the aggregate when the accumulation of capital has been pushed to the furthest point. This view has, of course, some plausibility; for admittedly inequalities of wealth and income are greatest in the richest Societies, and these have also the highest real wages. But it does not follow that the high productivity on which this wealth is based is the product of economic inequality, or that unrestricted inheritance is necessary to its maintenance.

It may, however, be admitted that any severe restriction on the right of inheritance would, unless the State used the proceeds as capital, reduce the rate of capital accumulation. The question is to what extent, and for what reasons, it would have this effect. Directly, it would take away a certain amount of capital that would have been used as the basis for creating more, and apply it to current spending. So much is obvious: the question is how far severer taxation of inheritance would react on the individual's will to accumulate.

That high inheritance taxation stimulates gifts *inter vivos* is evident enough. That it does not have this effect in a far greater measure is a clear sign of the tenacity with which the ageing tend to cling to their money. Most of them remain unwilling to surrender ownership or control to their children, except on a small scale, despite the possibility of avoiding a good deal of taxation. This bears out the point that, in general, the psychological incidence of taxation is upon the inheritor and not on the testator. This may not be the case where the testator insures against death duties, with the object of keeping intact a family business or a landed estate. But even insurance often comes out of what the insurer would have saved, and not spent, if he had not insured; and in that case the incidence remains upon the inheritors.

This point has obviously a bearing on the effect of inheritance taxation on the will to accumulate capital. For if the psychological incidence of the taxation is upon the inheritors, and not upon the original accumulator, it seems reasonable to suppose that taxes will not much affect the will to save. They may, indeed, positively increase saving, where the testator's object is to leave a business or property intact to his heirs. But this is not the most typical case. It is, however, highly relevant to point out that, among the richest members of a community, saving is largely automatic, in that it represents surplus income beyond the desire to spend. Clearly, saving of this sort will not be affected by taxation, save to the extent to which gifts *inter vivos* and charitable donations may be stimulated.

In the case of small fortunes, taxes on inheritance, where they exist at all, are usually at a low rate, and unlikely to affect saving, though they may to some extent divert it to forms of saving that are exempt from taxation, such as life insurance policies. It is mainly upon the accumulations of the larger savers that any effects of taxing inheritance are likely to be concentrated; and, as these are the most automatic, the effect upon them will probably be much less than is commonly supposed. Graduated taxes on large incomes, by reducing automatic saving, react far more decisively on the volume of accumulation than death duties.

It seems clear, then, that in Societies where property is very unevenly divided, the taxation of inheritance can be pushed to considerable lengths without much reaction on the volume of saving, and even without causing very much evasion, though some must be caused, by means of gifts *inter vivos*. But it is not suggested that there are no limits to this process. If a State, merely by steepening gradually its taxes on inheritance, sought by stages to abolish inheritance altogether, it would reach a point, far short of actual abolition, at which the taxation would react sharply on the volume of saving. Accordingly, any State pursuing such a policy would have to take steps, in the course of it,

to bring into being alternative methods of capital accumulation on a collective basis, and would have to apply the product of its inheritance taxes as capital and not as income.

It is, however, sometimes suggested that this difficulty could be avoided by adopting new methods of taxing inheritance, so as to allow full freedom of bequest for a single lifetime, with the proviso that all the property a man had inherited would pass to the State at his death. Or sometimes two lifetimes are suggested, with a heavy tax of, say, 50 per cent at the end of the first life, and the escheat of the balance to the State after the second life. There are many variants of this plan, which was first advanced by Professor E. Rignano, and has found distinguished support. The idea behind it is that few testators' desires to pass on property extend beyond one or, at most, two lives, and that accordingly a tax of this sort would have no deterrent effect on saving. It is further argued that full scope would be left for the development of business initiative with the aid of capital, and for the aggregation of capital into large units. Some of the adherents of the Rignano idea contemplate the ultimate disappearance of inheritance altogether; but this is not essential to it. It is consistent with a belief that the system of private enterprise ought to be maintained. At any rate in some of its forms, this plan of inheritance taxation, drastic as it is, is not of necessity anti-capitalistic. It has been urged by believers in Capitalism who wish to give more scope to personal initiative in the accumulation of wealth by removing hereditary inequalities.

Plans for the abolition of inheritance, on the other hand, are necessarily anti-capitalistic; for they involve either direct collective operation of capital resources, or collective control and rationing of their use. They are not necessarily Socialist; but they do imply the supersession of Capitalism as an economic system. It is not possible to advocate the abolition of inheritance on purely ethical grounds without being prepared to suggest alternative

methods for the accumulation of capital; and to this difficulty Socialism presents the most obvious answer. Moreover, if inheritance is abolished, or even if taxation of it is pushed very far, it becomes inevitable for the State as the taxing authority to take over actual assets; for beyond a certain point the proceeds of inheritance taxes could not possibly be collected in money. The State, then, would become in effect the heir; and it would be difficult to avoid the conclusion that the State should administer the assets acquired by way of taxation.

The economic and the ethical aspects of the question are thus closely intertwined. Many persons who are not prepared to defend inheritance directly on ethical grounds nevertheless uphold its economic desirability, because they mistrust the effects on production of an approach to Socialism. They may be ready to advocate the taxation of inheritance up to the point at which they think it will interfere with the private accumulation of capital; but beyond this they cannot be drawn by purely ethical considerations. This was in essence Bentham's position; and it has still powerful upholders in the world to-day.

To many other persons, the ethical arguments, which are directed partly against inequality in general and partly against inequalities resulting from inheritance and not from a man's own exertions, constitute a strong inducement to consider favourably any economic system which will make these inequalities unnecessary. The case for Socialism, which is based on a mingling of economic and ethical considerations, gains here a powerful reinforcement; for it can be pointed out that what the legatee in fact inherits is not a sum of money, but essentially a claim on the productive capacity of Society. This capacity, the result of centuries of development, is in reality a social product—the common heritage of civilisation, in which it would seem that all are entitled to share. In other words, when a man saves under present conditions, the result is to secure to him much more than he saves, because he acquires a preferential share in the social heritage. It seems unfair that a

man should be able to pass on this preferential claim to his successors without limit. Most States have passed legislation to prevent 'perpetuities', and to limit testators' rights to prescribe for generations ahead how their money is to be used, or to order that it shall accumulate at compound interest for a long period. But, in spite of these restrictions, there is nothing to prevent the claim itself from being perpetual; and this seems to many people to be manifestly unjust.

It is, indeed, true that capital does not in most cases survive for ever in an unbroken line of succession. Physical instruments of production, except land, wear out; and even where the capital they represent is perpetuated by the provision of adequate allowances for depreciation, there are hazards which do, in the long run, bring the life of most forms of business enterprise to an end. Even States, though they cannot go bankrupt, do sometimes repudiate their debts, and so confiscate the property of their bondholders; and, apart from the wasting of the assets themselves, there is likely, at some point in a long succession of heirs, to arise a wastrel who will dissipate his patrimony. It is indeed often stated that the life of most inherited fortunes is not long, except in the case of landed estates; and this is probably true, if it is meant that large fortunes are seldom kept together for many lives in the hands of a succession of sole heirs. There is a tendency to division of fortunes, as well as to wastage; and this tends to become more pronounced as property can be more and more easily divided through the operation of the joint stock system. But property rights are none the less perpetuated because they are divided up; and, as we have seen, the division does not make strongly for greater equality, because the property, even if it is divided, is usually left in the main to persons of the same social class.

It is doubtless possible to imagine a form of Socialism, or at any rate Collectivism, that would perpetuate inheritance much in its present form. If the State carried on industry, borrowing the money from its citizens, as it

borrows now in the case of nationalised or municipalised undertakings, inheritance could continue, the inherited property taking the form of perpetual State bonds or stocks. It is, however, difficult to imagine such a system being of long continuance; for it would clearly render the private owners of the capital completely functionless—mere receivers of interest or dividends, with no claim to income based even on a show of service. Under such conditions, they would certainly before long suffer expropriation; for no economic or social institution can survive permanently if it has lost the function which it came into being to perform. Socialism of this type would end, though it had not begun, in the abolition of inheritance, or in its restriction to things other than claims arising out of loans to the State.

Belief or disbelief in the institution of inheritance is therefore in effect very closely linked up with belief or disbelief in the private ownership and operation of the instruments of production. The abolition of inheritance, or its limitation to personal possessions of use, is in practice, if not necessarily in theory, a Socialist doctrine. Peculiar interest therefore attaches to the handling of the problem in Soviet Russia, where almost the first step of the new Government, in 1918, was to decree the total abolition of inheritance. This attitude has since been modified, and inheritance is now recognised under a decree of 1926. Direct descendants and widows are entitled to share in a dead person's property; furniture and household effects go to the housemates of the deceased; wills can be made so as to vary the disposal of property among the legal heirs, but not so as to leave it to others; and in the absence of testamentary provision, distribution among those entitled to benefit is equal.

Russia thus seems to have restored the right of inheritance taken away in 1918. But in fact the new provisions mean far less than would appear: they are indeed rather the result of the Communists' success in destroying private property than any token of a reversal of ideas or policy.

The Soviet Government can now afford to permit inheritance, because it does not permit the accumulation of wealth in private hands, and because, where accumulation does exceptionally still occur, it has plenty of other methods, besides the prevention of inheritance, of breaking it up. The private trader or the *kulak* (rich peasant) who succeeds in amassing property has no security at all of being able to retain it for his own lifetime; and the question of his right to pass it on to his descendants therefore loses most of its importance. The one form of private property which has hitherto remained in being is now being rapidly destroyed by the placing of agriculture on a collective basis, and, when that has been completed, the citizens of the Soviet Union will have no more than personal possessions to leave, except for the continuance for the time being of a small quantity of State bonds. For the Soviet Union does still, to a small extent, supplement the collective supply of capital by borrowing from its citizens.

This shows that, when a transition from Capitalism to Socialism is made abruptly, and accompanied by a general confiscation of existing wealth, the question of inheritance ceases at once to possess much economic importance; for both the existing capital and the power of fresh private accumulation are taken away at a blow. Moreover, to the extent to which private accumulation does survive for a time, it is more likely to be attacked by the direct confiscation of property from living owners than by the removal of the right of bequest or inheritance. There is still inheritance in Soviet Russia, but there is no problem of inheritance; for no one has enough to leave for inheritance to become a source of economic inequality. And, if this danger did arise in any case, the Soviet Government could easily root out the 'nuisance' by direct confiscation.

Inheritance is therefore essentially a problem of capitalist Society; and it cannot be abolished or restricted within narrow limits, so as still to leave capitalist Society intact. For if private persons are not to inherit, the State must; and State inheritance means State control of the use of

capital. Propaganda for the abolition of inheritance is in most cases in effect propaganda for Socialism; and the question of inheritance—as distinct from taxation of it within limits that will not destroy its essential character—thus merges in the wider question of a Socialist *versus* a capitalist framework of Society. The question is judged, not on its own merits, but mainly on those of the rival economic systems which different solutions of it connote. This is why there has never been any important social or economic movement making the abolition of inheritance its main objective. For those who favour this solution, on whatever grounds, must favour much more besides, in that they must be prepared with an economic reconstruction of Society that does not involve inheritance on any significant scale.

But, if it is impossible to abolish inheritance without altering profoundly the economic structure of Society, it is no less out of the question to retain inheritance in anything like its present form if that structure is radically altered in a Socialist sense. For inheritance is bound up with the divisions of Society into distinct social and economic classes, and influences this division the more profoundly because, in advanced communities, the better-off classes tend to have lower birth-rates than the poorer sections of the people, and therefore to keep their wealth within a narrow range. The institution of inheritance helps indeed to foster this control of numbers among the well-to-do; for they are conscious of the need for limitation as a means of preserving their class status. Even where primogeniture remains the custom, this limiting influence holds good; for the disinherited younger children fall due to be provided for during the testator's life, by expenditure on education and training, by enabling them to start in business, or by marrying daughters off with at least some 'portion' of their own. It is true that the growth of feminism has tended to some further diffusion of property; for daughters are now more often than before treated on an equality with sons. But this may even accentuate the tendency towards

family limitation among the classes not rich, but comfortably off.

In fine, then, the future of inheritance appears to depend on the one hand on the growth, in modern communities, of collective methods of capital accumulation and of the control of business resources, and on the other on the pressure of the popular movement towards a less unequal distribution of incomes. For this movement, ethical as well as economic in its driving force, results in forms of taxation which limit saving and impinge on profits, and thus leads to the necessity for alternative methods of saving and of ensuring adequate production. The two influences thus meet and mingle; and it is not easy to see how the institution of inheritance, save in a greatly modified form, can indefinitely stand out against them.

To the extent to which inheritance is restricted, there is a return from the individualistic notion of property to a communal notion, based now on a wider unit not only than the family, but than the class or tribe. For property comes to be regarded as part of the social heritage of the modern community, legitimately charged with the maintenance of all the members. This notion may further undermine, as it has already undermined in Russia, what remains in industrial societies of the conception of family solidarity. It will inevitably affect the institution of marriage, and the relations between parents and children. But even in capitalist Society the family has largely lost its economic significance, and become, save in respect of inheritance, mainly a social unit, whose bonds have grown far less tight even within living memory. If inheritance goes, the last economic bond will be snapped, at any rate beyond the period of the children's upbringing. And that too is likely to become increasingly a social function.

Nevertheless, the institution of inheritance remains for the moment strong, despite ethical assaults upon it. For it cannot be superseded except by the inauguration of a different system of accumulating capital and producing wealth.

XII

ECONOMIC MOBILISATION [1]

THIS essay is intended to be a survey of the problems of mobilisation and demobilisation chiefly from the economic point of view, that is to say, in relation to their reactions on the organised economic life of communities in war-time, the use of national man-power and other economic resources, and the effects of war on the subsequent organisation of industry and commerce. It will deal only incidentally with military mobilisation and demobilisation as far as these questions are essential to an understanding of the economic factors.

The entire conception of what mobilisation involves has obviously been altered in a radical sense by the events of the World War. Even before 1914 there had been, especially after the Franco-Prussian War of 1870, a growing disposition to realise that in any future war between the leading Powers mobilisation would have to extend over the greater part of the national man-power and would involve a substantial interference with the normal economic life of the nation. The development of large conscript armies, accompanied by a rapid growth in the elaborateness and cost of military equipment resulting from the advance of technical knowledge, had made obsolete those theories of mobilisation which were conceived in terms of relatively small standing armies provided with an equipment which could be supplied without any strain on the general economic systems of the belligerent countries. But side by side with the growth in the scale and complexity of armaments there had grown up in many people's minds a firm belief that future wars were certain

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to be short because the issue would be decided almost at the moment of the first onset, and because it was thought to be impossible for nations to stand for any protracted period the human, economic, and financial strain of modern warfare. Emphasis had therefore been laid in the drawing up of plans of mobilisation rather on speed of movement and the quick placing of a large and well-equipped and trained army in the field than on the supply of this army with continuous drafts of reinforcements and a continuous stream of fresh munitions and engines of war. The conception of a small standing army fighting its battles with comparatively small reactions on the way of living of the nation as a whole had indeed given way, at any rate in France and Germany, to the conception of a nation in arms. But the nation in arms was conceived far too much, as events proved, in terms of military man-power and far too little in terms of equipment and of the maintenance of production behind the lines to meet the needs both of the armies and of the civilian populations. In Great Britain, indeed, the conception of the nation in arms, despite the life-long advocacy of Lord Roberts, had made no general conquest even of military opinion; and the predominant view in Great Britain in 1914 was still that the British function in a world war would be that of keeping the seas and of throwing into the conflict a small and highly trained expeditionary force capable, in collaboration with the larger armies of its allies, of turning the issue at the first encounter. In Great Britain equipment had been thought of in the terms appropriate to a small professional army of this type, and hardly at all in terms of an army running into millions of effectives.

It is true that this question of the nation in arms had been raised in an active form more than a hundred years before the Great War, at the outset of the war of defence waged by revolutionary France in the years immediately following the Revolution of 1789. At that time the French found themselves threatened by hostile armies on all their frontiers, and in imminent danger of military collapse.

Their first thought was to augment their forces in the field by the method of the *levée en masse*; that is to say, by calling to the colours every able-bodied man who could be mobilised; and plans for the *levée en masse* were seriously debated and began to be carried out. It was, however, speedily realised by the Second Committee of Public Safety that the *levée en masse* would be utterly fruitless unless provision were made for the supply of the armies in the field with an adequate quantity of munitions of war, and that the available munitions were in fact far below the requirements even of the armies already in active being. In these circumstances the Committee of Public Safety set to work resolutely, in place of calling the entire man-power of the nation to arms, to organise the supply of munitions of war. This task was rendered the more difficult both because France had been largely dependent on imported iron and steel and because some of the most important metal-working establishments were near the frontier districts, and had fallen into the enemies' hands, while others were under the control of persons whose loyalty to the new Republic was at the least suspect. Prodigious efforts were made both to collect available stores of metal and to teach steel-making processes to workmen hitherto unaccustomed to their use, and to mobilise for industrial service workmen from a variety of occupations whose skill could be adapted to the making of munitions of war. The great centre of the new manufacture was at Paris; but commissioners were also sent throughout the provinces to aid in the reorganisation, to bring about a reconstruction in the existing establishments such as those of Le Creusot and Indret, and to bring new establishments into existence. With the aid of these measures, which were carried through with extraordinary expedition, the French armies were so re-equipped that they were able to roll back the invaders beyond the frontiers and before long to penetrate well beyond the boundaries of revolutionary France. At first, while these advances into new territory were still regarded as

precarious, every effort was made to destroy radically all establishments suitable for the manufacture of armaments in the occupied territories, the plant and available materials being carried back for use in France; but at a later stage, particularly in the case of Belgium, great efforts were made to use the occupied areas for the production of an additional supply of munitions, and it is well known that Belgian industrial development is closely connected with the use made of Belgian productive resources for this purpose during the French occupation. At the same time the French engaged in a vigorous contraband trade in the smuggling in of raw materials and of munitions from beyond their frontiers, large quantities being obtained from Germany *via* Switzerland in the early years of the Revolutionary Wars. The lesson that the nation in arms is a meaningless expression unless there is a proper balance between the mobilised man-power and the supply of munitions and commissariat would thus seem to have been driven home by the experience of France in the Revolutionary Wars. It had nevertheless been largely forgotten even by the French themselves before 1914; or rather, the French conceived that modern wars would be waged under very different conditions, and therefore adopted what turned out in the event to be a mistaken view of the essentials of military preparedness.

It is appropriate at this stage to attempt a brief review of the position and attitude in 1914 of the leading European Powers which were then on the brink of war. In France more than in any other country the doctrine that success was likely to depend on swift offensive action by a large trained army capable of very rapid movement held the field and had been made the basis of military preparation. The aim of the French military service system, based on three years' conscript service followed by a period in the reserve, had been to provide, in face of the deficiency of French man-power in relation to that of Germany, the largest possible trained force that could be thrown immediately into the field. As this force was thought of as

essentially an offensive body, its equipment had been designed rather for swiftness of movement and action than for the type of trench warfare which became predominant within the early months of the war. Moreover, as the issue was thought of as depending primarily on the outcome of the first offensive, comparatively little thought had been given either to the use and equipment of second-line reserves or to the maintenance of a continuous supply of munitions and other requisites for the armies in the field. The French idea was essentially that of a swift advance into the enemy's territory leading up to a quick decision before the superior reserve man-power of Germany could have time to take effect.

The Germans on their side shared in full the French view of the importance of taking the offensive, and realised that their situation made this imperative, because, if operations were once allowed to proceed upon German territory, the areas in which their coal mines and metal works and engineering establishments chiefly lay, being near the frontiers, would be likely to be put out of action. They, too, had therefore endeavoured above all to provide themselves with an army well equipped for taking the immediate offensive; but far more than the French they had understood the possibility not only that the war might be protracted, but also that they might find themselves, by the British command of the seas, cut off from external supplies and compelled to depend upon their own economic resources. This had led them to pay considerably more attention than either the French or the British to the economic aspects of preparation for war. Even they had by no means realised in advance either what the duration of the war was likely to be or the enormous calls which it would make on other industries for the equipment of the armed forces. The chief difference in the German and the French preparedness lay in two things—first, in the greater emphasis which the Germans had placed before 1914 on the economic side, and secondly, in their more effective use of their trained reserves, whereby they were able to bring

their superiority in man-power immediately into play by creating at once new units based on these reserves, thus duplicating the whole of the conscript army actually in service in time of peace. Alone among the Powers they had realised that, given a large body of highly trained officers and technical personnel and a sufficient initial equipment, it would be possible to use reservists at the very outset of hostilities as an offensive force side by side with the personnel already in arms. These two things were indeed the very foundations of the initial German success. The magnitude of the forces which Germany was able immediately to throw into the front line upset all the French calculations and placed the Franco-British forces immediately upon the defensive—a strategy which their previous preparations rendered singularly disadvantageous to them.

Of the other European belligerents, it is only necessary here to add a few words about Russia. Russia possessed a large army and enormous reserves of man-power; but she was singularly deficient both in technical equipment and in trained leadership, while even her high command was riddled with corruption and nepotism. Moreover, being far less industrialised than the Powers of Western Europe, she was from the first far more largely dependent on her allies for munitions and equipment, and thereby far less able to improvise the necessary supply services by the transformation of her industries to meet war needs.

When the United States entered the war in 1917 her situation was not unlike that of Great Britain in 1914. The United States had a small professional army but even less than Great Britain any commensurate trained reserve. She had vast industrial resources; but almost nothing had been done in advance even to consider the use of these resources for the purposes of war, though in practice the large growth of her exports to the Allied countries between 1914 and 1917 had prepared the way for the rapid transformation of her industrial system to a war basis. It was consequently possible very rapidly to adapt the industries of the United

States to a hugely increased output of war supplies; and as, by the time the United States entered the war, the chief problem of the Allied countries was coming to be a serious deficiency of man-power, both for filling up the gaps in the fighting forces and for keeping their industries at work, the task set before the United States was from the outset reasonably clear. She had as speedily as possible to train a large new army to fill up the depleted ranks of the fighting forces in Europe; and she had meanwhile so to increase her output of supplies as to enable her European Allies, by depending more on her for war supplies and for meeting the needs of their civil populations, to release more of their industrial personnel for military service.

It will be understood from what has been said that all the belligerents who entered the war in 1914 had radically to alter their conceptions within a few months of its beginning, and that this was especially true of France and Great Britain. The checking of the great German offensive short of Paris brought home to the French high command the probability of a protracted defensive war, involving the occupation of a long front extending the whole length of French territory from Switzerland to the sea. The defence of this line was obviously bound to involve an enormous expenditure of resources on the provision of the necessary munitions and transport, as well as the mobilisation and equipment of a vast army for a protracted period. But the German offensive had been successful in occupying and thus putting out of action a large sector of French territory in which lay a considerable proportion of France's industries, particularly of her heavy industries. While, therefore, efforts were made rapidly to develop new sources of supply by the use of the industrial resources still remaining behind the French lines, a far larger share than had been originally anticipated of the task of keeping the Allied armies supplied with war equipment necessarily fell on the metal and engineering industries of Great Britain. Until the supplies from the United States began to come in, Great Britain was called upon to play the chief part in supplying

munitions of war not only for her own rapidly growing forces but also for her Allies.

Even in these circumstances it was some time before any drastic reorganisation took place in the British heavy industries in order to fit them for this service. For some time after the outbreak of war the War Office continued to rely, in placing its orders for munitions, on the few Government factories and on those contractors who had been regularly engaged in supplying armaments before the war. Tenders from outside firms were at first considered only with great reluctance; and no attempt was made until the early months of 1915 to mobilise the available engineering resources for the supply of munitions—much less to build new factories with that end in view. Originally the whole question was left in the hands of the War Office, and it was not until March 1915 that a distinct and semi-autonomous organisation was set up inside the War Office to take control of the supply of munitions. Out of this special department of the War Office grew, in the summer of 1915, the Ministry of Munitions, as a separate Government department with a political head of its own occupying a seat in the Cabinet. Some attempts had been made earlier in the year to speed up the output of shells and other munitions of war by creating in various parts of the country Armaments Committees representing employers and Trade Unions, and by establishing a Committee on Production to lay down general lines for the development of the munition services in their relation to labour. This body had advanced proposals for the improvement of time-keeping, for the relaxation of Trade Union restrictions for the duration of the war only, and for the enrolment of women to fill up the gaps caused by the enlistment of male workers and to increase the total output. When the Ministry of Munitions was established in 1915 the Armaments Committees were allowed to fade out of existence, the Committee on Production became merely a body for arbitrating on wages and conditions of labour, and the work of organising the munitions services was taken over directly by the Ministry. The

Munitions of War Act, passed in July 1915, established compulsory arbitration in the industries providing war supplies, prohibited strikes and lock-outs, and provided locally for the suspension of Trade Union restrictions. At the same time it set up a system of 'controlled establishments'—that is to say, of factories scheduled for the production of munitions. These factories were brought under direct Government control, under a system by which their profits were limited and the greater part of any excess profits made in consequence of the war was to pass directly to the State. This Act applied not only to engineering and metal-working establishments but to any industry directly engaged in producing substances 'intended or adapted for use in war'. Thus, when the South Wales miners struck in the summer of 1915 the dispute was at once proclaimed under the Munitions of War Act and settled by compulsory arbitration. The system of 'controlled establishments' was, however, limited to engineering, shipbuilding, and other metal-working firms, and was not extended to cover either the coal industry or such industries as the Yorkshire woollen trade, which were also engaged in producing munitions in the wider sense. The coal trade was not brought under any complete Government control until the advent of the Lloyd George Government in 1917; and the woollen industry continued to be regulated under a department of the War Office dealing with contracts.

The Munitions of War Act of 1915 was the first comprehensive attempt at the regulation of industry under State control. It was, however, in the early stages of the war, so administered as to involve as little interference as possible with the British traditions of private enterprise and *laissez-faire*. Firms were instructed to carry on as usual, apart from any special regulations made for them under the Act; and, so far from simply commandeering the various establishments, the Government continued to make contracts with them in respect of each particular order for goods. At this stage the entire emphasis was on speed of supply rather than cost, and many of the con-

tracts made with munitions firms in 1915 and 1916 were on an exceedingly extravagant basis. Often the form of contract was that of 'cost plus profit' rather than 'fixed contract price', and there were the widest possible divergences between the prices paid for the same types of supplies to different establishments. Gradually, however, factories which had been attempting to make munitions of war with highly unsuitable plants were enabled or compelled to install special machinery and to build new works and sheds for the expansion of war output; and as the Ministry of Munitions gained experience 'cost plus profit' contracts were gradually superseded by a much stricter system of regulation, especially as it became more and more plain that the prolongation of the war would make the question of its cost a far more vital matter than had been at first supposed. During 1916 the system of regulation was being gradually tightened; but it was not until 1917 that control was anything like complete.

At the same time the problem of labour supply was becoming more and more acute. In the Act of 1915 provision was made for the enrolment of a class of workers known as 'War Munition Volunteers', who were invited to enrol for special service and were thereafter transferable to any factory where the Ministry of Munitions considered their services to be specially needed. At this time Great Britain was still working under a system of voluntary military service; and the entire position was changed with the advent of military conscription. This came by stages, beginning with compulsory registration of all British subjects under the National Registration Act of July 1915 and the so-called Derby Scheme of October 1915, under which men were invited to 'attest'—that is, to offer themselves potentially as soldiers without any certainty that they would actually be called up. A vigorous campaign conducted under the Derby Scheme prepared the way for compulsion; and under the first Military Service Act of 1916 this was instituted for all men up to forty years of age on March 2, 1916, the scope of compulsion being subsequently

extended in May to include men up to fifty years of age. The introduction of compulsory military service at once involved the taking of decisions as to the number of men who could be spared from the munition works and from other industries for enlistment as soldiers; and side by side with military conscription a system of 'starring' was introduced, whereby men who were 'starred' by the Ministry of Munitions or other responsible Government departments could be exempted from actual calling up. There was also under the Military Service Acts a system of Local Tribunals before which men could apply for exemption on occupational as well as conscientious grounds. Thereafter a substantial number of the workers left in industry were 'starred' men; but these were not placed under any form of military discipline or regarded as having been called up for military service. As the need for fresh recruitment to the fighting forces grew more pressing during the later years of the war, more and more 'stars' were withdrawn and exemptions on occupational grounds revised, and at the same time the standard of physical fitness required for military service was progressively lowered. By these means more and more men were 'combed out', until the great mass of the less skilled workers of military age had been taken out of the factories and of the original labour forces only those possessing a high degree of indispensable skill remained.

The gaps thus caused in the ranks of industry had of course to be filled up. This was done to a large extent by withdrawing workers unfit or over military age from the less essential occupations and transferring them to the essential industries, by the increased employment of women and young persons, and by progressive mechanisation designed to reduce the total demand for labour. But man-power in the munitions industries had also to be supplemented by other means. It was found that of the highly skilled workers an undue proportion had been taken away in spite of the unprecedented magnitude of the demand for munitions of war; and to some extent men had

to be recalled from the colours for industrial service both in the engineering shops and in the coal mines. At the same time men who had been so wounded as to be unfit for further service but were still suitable for industrial work were sent back to fill up the gaps in the factories and make possible the release of fresh workers. At first these returned workers were discharged from the army and worked as ordinary civilians; but at a later stage they were retained in the army reserve and went back to the factories as 'Army Reserve Munition Workers', liable to recall to the colours in the case of need. They were not directly subject to any military discipline in the factories; but their status as reservists necessarily reacted on their position in industry.

In France, with its previously established system of military service, the problem of man-power in industry became at an early stage even more acute than in Great Britain. In pursuance of their theory of a short offensive war the French began by calling up men almost without any regard to industrial requirements; and as soon as they had to settle down to prolonged trench warfare it became evident that large numbers of those who had been taken away would have to be returned to industry if production was to be kept up on the requisite scale. Accordingly a system of requisitions from employers for men who had been enlisted was introduced, and very large numbers of men were returned from military service under this scheme, retaining the status of reservists liable to recall in case of need. In the later stages of the war France introduced a system of discharging from further military service the surviving members of those families which had suffered exceptionally heavy losses in the war, and this release of men provided a small additional flow of workers back into industry and, more especially, agriculture.

In Germany, as we have seen, steps were taken immediately upon the imminence of war to double the effective strength of the army already in service by the formation of reserve units; and at the same time men were called up to

create a further reserve for the filling of gaps in the ranks. Measures were also taken immediately to organise German industry in face of the shutting off of supplies from outside. A special administration was formed at the War Department under Walther Rathenau for the organisation of the supply of necessary raw materials as well as for research into the provision of substitutes for those materials of which a deficiency was certain to arise. Drastic steps were taken to requisition available supplies of materials and to set German industries at once on a war footing. In this respect Germany moved far more swiftly than the Allied Governments towards a system of rigid State control and economic mobilisation. Meanwhile the civil authorities were largely superseded by military administrations, and Germany was divided into a series of military areas each under the authority of a general responsible to the War Department. In 1916, as the problem of man-power and military and civil supplies became still more acute, a more thoroughgoing conscription of labour was instituted under what was known as the 'Hindenburg programme', including the so-called 'law of auxiliary services'. The militarisation of the 'home front' went so far as to provoke in 1917 a strong reaction on the part of German public opinion; and this necessitated some reassertion of the civil authority. But throughout the war the industrial mobilisation of Germany continued to be treated in effect as an aspect of military mobilisation under the control of the War Department.

In the United States the earliest measures of importance designed in view of the outbreak of war were the formation of the Council of National Defence in August 1916, and the setting up in March 1917 of the Munitions Standards Board, which became the General Munitions Board in the following month. This organisation, however, was soon found quite inadequate for the tasks imposed upon American industry, and eventually the central work of organisation was handed over to the powerful and far-reaching War Industries Board, which controlled for the period of the

war the entire productive activity of the United States, the buying, selling, and allocation of raw materials and of labour, and the facilities for transport by both land and sea. Under the control of this body were all questions of priority as between different claims. It had the responsibility of fixing prices for staple commodities, and it served as a co-ordinating body for the other agencies responsible for war-time industrial activities. Among these were the War Trade Board, the Shipping Board, and the Emergency Fuel Corporation, the special food administrations, the War Labour Board, the Allied Purchasing Commission, which was in charge of purchases on account of the European Allies, and the Railroad Administration, which took over and operated all the American railways as a single unit under complete Federal control. The War Industries Board derived its authority from the great emergency powers conferred upon the President of the United States for the duration of the war, and was able in the exercise of this authority to serve as a 'general staff' for American industry as a whole.

At the same time intensive efforts were being made to mobilise American man-power. The Selective Service Act came into force in May 1917 and provision was made under it for the immediate enlistment of one million men. By the end of the war this number had been raised to 3,365,000, of whom over two millions were actually in France. By the same date the number of workers, men and women, engaged in war work had risen to nearly nine and a half millions. The main problem in the United States was to strike the right balance between the sending of military units to fill up the depleted Allied lines in Europe and the organisation of an adequate supply of foodstuffs, munitions, and other requirements for the fighting forces and the civil populations of the Allied countries. In the main the policy adopted by the Allied and Associated Governments was that the United States should send to Europe as many troops as she could consistently with the maintenance of necessary supplies of foodstuffs and raw materials, and that the

Allies, who had by that time largely solved the problem of munitions supply, should help the American army with munitions of war, being enabled so to do by the release of men from active service as they could be replaced by American soldiers.

In addition to the effect of the war in rendering necessary a large degree of industrial mobilisation within each separate country, the need speedily arose for some general supervision over the production of goods in all the Allied countries in relation one to another as well as over the allocation of shipping space in accordance with the requirements of the different Allies. This control was naturally far less strict and far less exactly defined than the systems of control established in each individual country. But it produced a great effect in the correlation of inter-allied needs and resources. At the highest stage this inter-allied control was exercised under the authority of the Supreme War Council, which had the ultimate supervision over economic as well as military affairs. The Inter-allied Conference and the Inter-allied Munitions Council were more directly responsible, under the Supreme War Council's authority, for formulating the broad principles of inter-allied economic co-operation. For example, it was under their auspices that the countries at war concluded the Inter-allied Ordnance Agreement, under which at the beginning of American participation in the war the United States shipped large quantities of raw and semi-finished materials to England and France. The object of this was to avoid the delay which was otherwise bound to attend the building up of American war industries by making full use of the resources of the establishments in the Allied countries which were already equipped for the rapid manufacture of munitions of war. The allocation of shipping resources was also brought under a high degree of inter-allied control, which has been fully described in Sir Arthur Salter's well-known book *Allied Shipping Control*. In addition to the work done by the actual inter-allied Committees and Councils, many further measures of co-ordination were achieved by direct negotia-

tion and agreement between individual countries. Each of the leading European Allies, for example, kept a permanent mission in the United States; and these missions were in constant negotiation over matters of concern to the various countries.

Nor could mobilisation be confined to the military and industrial fields; it had also to extend to the field of finance. For it was necessary not only to arrange for the production of enormous quantities of war materials and other supplies and for their shipment to Europe, but also to devise methods whereby payment could be made to the suppliers of these goods. This problem had two aspects: it was necessary to increase and mobilise the supply of means of payment in the hands of the Allied Governments, and it was also necessary to direct the available monetary resources into the right channels. Funds for this purpose could be secured either by drawing upon the fiscal resources of the various nations through taxation or by borrowing in their domestic money markets or by creating new credit, either directly through the issue of paper money or indirectly by means of advances from a State bank of issue in the form of bank-notes. All the belligerent countries both added greatly to the amount of taxation and floated large loans which were taken up both by the general public and to a large extent by banks and other financial institutions. These methods were not without a great effect in raising the level of prices; for under conditions of war-time demand taxation was apt to be offset by higher profits, and bond issues were apt to be inflationary in their effects, especially when they were taken up either directly by the banks or by subscribers who obtained the money to pay for them by means of bank advances. Great Britain and the United States largely financed the war out of taxation and bond issues, whereas the other belligerent countries found themselves forced to adopt to a larger extent more directly inflationary methods of financing, either by issuing State paper money or by borrowing from their banks of issue. Moreover, all the Allied countries obtained large loans in

the earlier stages of the war from Great Britain and later from the United States. A large part of the British borrowing from the United States was in fact for the purpose of re-lending to the less solvent Allied countries, so that directly or indirectly the United States became the chief financier of the Allies, with Great Britain acting largely, on the strength of her superior credit, as an intermediary for passing on American loans to the needier countries.

So pressing was the need for funds for war purposes that all the belligerent Governments were compelled to take measures for the strict regulation of the movement of new capital within each country so as to divert new money from non-essential industries to those which were deemed to be necessary for the successful carrying on of the war and for the maintenance of the 'home front'. When the United States entered the war a special Capital Issues Committee was formed to supervise and regulate new security issues of all kinds. This function passed in 1918 to the War Finance Corporation. This Corporation, organised with a capital of 500,000,000 dollars advanced by the United States Government, had the additional function of extending new credits to essential industries, public utility services, and savings banks, which were thus enabled to give additional help to their depositors in taking up Government issues of bonds. Similar forms of control and assistance to private subscribers to Government loans were exercised by other countries. In addition, Great Britain, in order to make payment for her vast purchases in the United States both on her own and on Allied account, was compelled to take measures for the mobilisation of American securities belonging to British investors. These securities were taken over by the Government at a valuation, shipped to New York and sold, and the British Government was thus put in funds for meeting its obligations. This applies primarily to the period before the United States entered the war; for thereafter payment was made mainly out of loans raised on the American side of the Atlantic.

When the Armistice was concluded in November 1918

the various Governments were at once confronted with the problem both of demobilising the large armies on the Western front and of placing their industries which had been diverted to meet the needs of war once again on a peace-time footing. The Russian armies had, indeed, some months earlier, in Lenin's phrase, 'voted with their feet', and returned in disorganisation to their villages; but in the other countries demobilisation had to proceed in accordance with a regular plan. On the one hand the men were themselves for the most part overwhelmingly anxious to get home and exceedingly reluctant to submit to a continuance of war discipline when in their view the need for it had passed. But on the other hand not only did transport present considerable difficulties, but it was also certain that if the armies, apart from such forces as it was intended to retain under arms, were demobilised at once, there would for the most part be no jobs waiting for them when they got back, and serious social upheavals might arise as a result of their return before industry could be placed on a footing to receive them. The workers who had been brought into the war industries between 1914 and 1918 had to be transferred to a great extent to other jobs in order to make room for the returning soldiers; and the whole process of change-over in industry was bound to take time even if, as most people then supposed, there was likely to be work for all as soon as the necessary reorganisation had been carried through.

The technique of demobilisation had therefore to be based on a compromise. The demobilised soldiers were to be returned to civil life as speedily as there was any hope of absorbing them; but their anxiety to return home had to be curbed in order to avoid the dangers of civil disturbance either in the military units or at home. France had in this respect a simpler problem than Great Britain; for a large mass of her conscripts were agriculturalists who could for the most part go back at once to their holdings, and there was a great mass of work waiting to be done in the rebuilding of devastated areas. French demobilisation,

apart from the relatively large army of occupation retained in service, was therefore comparatively rapid; and even in the case of Great Britain demobilisation had to be speeded up beyond what had been intended in consequence of the growing difficulties experienced in keeping order in the military camps now that hostilities were at an end. This involved some form of provision for demobilised soldiers until they were able to find jobs, and it was also necessary to make provision for the discharged munition workers, whose transference to other occupations was bound to take time. For these purposes a system of 'donations' was introduced. Demobilised soldiers were entitled to draw, in addition to the gratuity accruing to them on discharge, a weekly donation benefit as long as they remained unemployed; and a similar 'donation' on a smaller scale was also provided for unemployed munition workers. This 'donation' system was thereafter gradually superseded by the introduction of a general scheme of unemployment insurance under the Act of 1920. Unemployment insurance had already been applied to a certain group of trades, including engineering and shipbuilding, before the war; and it had been extended over a wider field to cover a certain proportion of munition workers by an Act of 1916. But in the immediate post-war emergency the regular unemployment insurance scheme was left in suspense, and it was thought better, until it had been revised and placed on an inclusive footing, to make temporary provision for the unemployed by means of the ex-Service and civilian 'donation' schemes. By these means demobilisation was actually brought about without any serious degree of civil disturbance or industrial dislocation. This was largely due to the fact that during 1919 and 1920 there was a brisk demand for labour, and industry prospered, partly under the stimulus of renovation work urgently needed in consequence of the ravages of war, and partly because a rapidly rising price level due to inflation swelled industrial profits and induced employers to take on a rapidly increasing quantity of labour. The short-lived post-war boom

did not break until the later months of 1920; and by that time demobilisation had been successfully carried through, and the risks of civil disturbance inherent in it successfully overcome.

In the meantime the various forms of State control over industry which had been introduced during the war were being rapidly liquidated in most of the belligerent countries. There went up from employers on the morrow of the Armistice an urgent cry for a 'return to pre-war conditions' and for the immediate abrogation of State control of industry. Despite warnings that there were serious dangers in abolishing at once the elaborate systems of control which had been built up, the employers' demands were in most cases speedily conceded. Munition factories were decontrolled, and the industries which had been under the surveillance of the War Office Contracts Department also regained their freedom at an early stage. Shipping, too, was decontrolled, and the vessels which had been built directly by the State for service under the Ministry of Shipping were sold off to private firms. Only in the case of the coal-mines was it found necessary, on account of the extreme scarcity of coal in Europe and the need for preventing an abnormal rise in prices in the home market, to retain the system of control for a longer period. Government control of the coal-mines did not finally lapse until the spring of 1921, and then only after the great post-war slump had set in, to the accompaniment of an embittered dispute resulting from the cutting down of wages by the employers as soon as State aid to the industry was withdrawn.

Similarly in other countries the end of the war was the signal for an insistent demand from employers and traders for the abrogation of the various systems of State control which had been instituted during the war. Alike in France, Great Britain, and the United States the demand for a return to 'pre-war conditions' and to 'business as usual' was too powerful to be resisted by Governments which retained their belief in the capitalist system and, broadly,

in the philosophy of *laissez-faire* and private enterprise. Consequently the elaborate systems of control which had been built up during the war were rapidly scrapped, and the owners of industry regained in most respects their old freedom. The experience of the war years could not, however, be in practice so easily done away with. In the first place the various Governments, in order to mobilise economic resources during the war, had been compelled to call into being a far stronger organisation among the employers in the various industries than had existed up to 1914; and these employers' associations and combines, although they ceased after 1918 to act as agents for the Government or under the Government's orders, maintained their existence, so that in all three countries Capitalism emerged from the war far more highly organised and with far more tendency towards collective action than it had possessed hitherto. Moreover, in both Great Britain and France the effect of the war had been to strengthen considerably the Trade Union movement and the forces making for the enactment of industrial legislation. The workers in these countries were powerful enough to retain after the war part of the protective measures which had been adopted between 1914 and 1918 in the interests of industrial peace. The French Trade Union movement did, indeed, before long lose most of the strength which the war had added to it, owing to the internecine disputes between its Communist and orthodox wings. But in Great Britain and also in Germany a substantial part of the new code of industrial legislation became permanent, and Trade Union power was considerably enhanced. In the United States constitutional difficulties stood in the way of any considerable development of industrial legislation, and the Trade Union movement there profited far less from the war than the movements in the European countries. The return to *laissez-faire* was most complete in the United States and least complete in Germany.

In Germany, indeed, the circumstances of the post-war years compelled the State to retain a large measure of con-

trol over industry. German post-war economic policy was influenced largely both by the terms of the Peace Treaty, which compelled the Government to keep a tighter hand on economic development, and by the internal situation, which gave right-wing Socialism a large measure of influence in framing the legislative code of the new German Republic. Nor was there in Germany the same traditional belief in *laissez-faire* as in other countries. In consequence of these facts, the war-time organisation of industry pioneered by Rathenau largely survived in the State recognition and organisation of cartels, as well as in the industrial legislation of the immediate post-war years.

Moreover, in all countries the lessons of economic organisation during the war struck deep roots in many people's minds; and even where employers and traders were strong enough to force an almost complete abrogation of war-time forms of State control, the war left behind it as a legacy the idea of organised national planning, which has since found more startling expression in the two Five-Year Plans of the Soviet Union. Capitalists themselves became readier to recognise under post-war conditions the need for organised planning; and by many non-Socialist advocates of various forms of planning, projects to be carried through as part of a general scheme for the rationalisation of industry were put forward from time to time. Except in Germany, these ideas have not borne much practical fruit; but they are undoubtedly much in men's minds, the more prominently because of the successful establishment of Socialist planning in Russia.

Ideas of military mobilisation as well as of economic organisation have been fundamentally changed by the World War. But in this case it is far more difficult to state clearly or simply what the outcome of the war has been. Under the terms of the Versailles Treaty, Germany was compelled to disarm, to abandon conscription, and to limit herself to a small standing army, as well as to a rigid limitation of her naval strength. With this provision of the Versailles Treaty was coupled a promise on the part of the

Allied Powers to disarm as well, so that, as armaments were progressively reduced, the restriction imposed on Germany would cease to be exceptional or punitive, and would fit in with the new and reduced standard of armaments to which all countries were to be asked to pledge themselves as an earnest of their desire to abolish war. Generals, however, remained sceptical of the strength of the League of Nations or of the efficacy of the various post-war pacts as means of preventing war; and, outside Germany, armaments still remain at a level enormously above that which was contemplated when the Versailles Treaty was signed. It follows that military plans of mobilisation have continued to be conceived in terms of possible future wars on the same scale as that of 1914, and therefore involving the complete mobilisation of national man-power, both military and economic. In these plans, far greater stress is now laid than before 1914 on the probability of any future war being protracted and exhausting, and, in the sphere of munitions, on the indispensability of a rapid mobilisation of productive resources for the supply not only of tanks, aeroplanes, and other engineering products but also of those gases with which no nation really believes that any other will, when the time comes, be prepared to dispense. The economic aspects of mobilisation therefore receive in military quarters far more attention than before the war, and the close relationship between military and industrial mobilisation is more clearly appreciated. Indeed, it looks as if the next war would go much further than the last in abolishing the distinction between combatant and non-combatant, and bringing the whole territory of the countries involved effectively within the sphere of active military operations.

XIII

THE ECONOMICS OF ADVERTISING

Is advertising waste? That familiar question can be asked or answered from two quite distinct points of view—from the standpoint of the individual advertiser, and from that of the community as a whole. We may mean, when we ask it, 'Does it pay the individual producer or salesman, or a group of co-operating salesmen, better to advertise, or not to advertise, their goods?' Or we may mean, 'Does advertising, from the standpoint of the community as a whole, tend to add to the costs of producing goods, and so to raise their price?' The two questions are widely different, and it is important at all times to be clear which of them we mean.

The first question, of course, cannot be answered at all in general terms. It all depends on what is advertised, and where and in what circumstances it is proposed to advertise. Take an extreme case. There is, in a particular district, only a single undertaker, who therefore gets all the custom available. Clearly he cannot by advertising his services cause more people to die, or attract more custom. People will come to him when they need him; and their demand for his services is fixed by circumstances beyond his or their control. He would be a fool to take a column in the local weekly paper in order to attract custom. But now a second undertaker comes to the town, opens premises in the main street, takes a column in the local paper, and sends out attractively designed business cards as soon as a death is reported. The original undertaker, who perhaps lived in a back street before, may think it best to take more noticeable and expensive premises in the main street—which is really a form of advertising—to pay for space in the paper, and to set out to canvass for clients. And he

may be driven to do this all the more for precisely the reason that made it quite useless for him to advertise before—because the amount of demand for undertakers' services is strictly limited, and accordingly every customer gained by his rival is so much loss to him.

Now, this looks at first sight as if advertising were a product of competition. So it is, to a very great extent. But it is not wholly so. Take another case. There is but one cinema in the district of which we are speaking. But it may still be worth the proprietor's while to advertise, despite the absence of competition. For the demand for the service of the cinema is not, like that for the undertaker's, fixed in amount. The cinema wants to attract people to spend money there instead of spending it on something quite different—on books, or chocolates, or a new tablecloth, or a pair of boots, or what not. The cinema proprietor wants to make his house, and the attractiveness of his programmes, widely known. If he hires an expensive film, featuring Charlie Chaplin or Mary Pickford, or some other celebrity, he is likely to spend more on advertising in the particular week when that picture is showing. If a rival cinema opens in the town, that will tend to make him advertise more; for people's incomes are limited, and a good many will make choice between the rival shows. But even in the absence of all competition in his own line of business, he will almost certainly advertise to some extent, both in order to make his programmes known and in order to suggest as strongly as he can to as many people as possible that the cinema is a good way of spending their money. In the phrase of the economists, the demand for undertakers' services is totally *inelastic*, whereas the demand for moving pictures is *elastic*. It therefore pays to advertise, at least to some extent, in the one case and not in the other, even in the absence of any sort of competition.

The cinema is, indeed, an excellent case for illustrating the expediency of advertising, from the standpoint of the advertiser himself. It is built to hold up to a certain number of people, in seats carrying various prices. The cost of rent-

ing and showing the film and the other costs of the service are practically unaffected by the number of people who come to the show. The cost per customer is therefore small practically in proportion—allowing for differences in the price of seats—as the number of customers is large. The position is not quite the same in manufacturing industries; for the cost of producing two thousand articles is certain to be larger in the aggregate than the cost of producing one thousand. But in most modern processes of manufacture, the cost of each article produced tends to fall, often very sharply, as the number of articles is increased. The more mechanical the industry, the more certain is this to be the case. Modern plants are built so as to work most economically at a certain level of output. Their capital and running costs are high, and can be carried so as to leave a good margin of profit only if they can be run up to their full capacity. If they are compelled to work short time, their costs are often higher than those of less up-to-date and less highly mechanised plants. Accordingly, their owners have a strong inducement to get enough custom to keep their works fully employed. This leads to all sorts of practices (export dumping, for example) which it falls outside the scope of this paper to consider. And it also tends to lead to advertising wherever the demand for the product in question is elastic, in the sense given to the term above, or wherever, though the demand is inelastic, there is a possibility of attracting trade away from a competitor.

This situation is generally expressed by economists in the phrase 'decreasing costs' or 'increasing returns'. An industry or process is said to work under conditions of decreasing costs or increasing returns when the unit cost of production tends to fall with an increase in the quantity produced. Pure handicraft trades tend to work under conditions of practically constant cost: almost all highly mechanised trades work, at least within certain limits, under conditions of decreasing cost. The growth of mechanisation in industry has therefore been a powerful factor in stimulating the process of advertisement. That is partly

why advertisement has been pushed furthest in America, which is also the country of greatest mechanisation. American industry is, however, despite the prevalence of combines, also highly competitive; and this is a no less powerful reason for the great growth of advertising in the United States.

I have been speaking so far of advertising in general, without attempting to distinguish between its various forms. But, of course, it matters very much where and how advertisement is done. Take first the case of newspaper advertising. It is of little use to ask in general whether newspaper advertising pays the advertiser. It all depends what he wants to advertise, and where he advertises it. If a publisher took a full page of the *Daily Mail* in order to advertise a volume of poems by Mr. W. B. Yeats, everyone would say he was mad. But even a large advertisement of such a book in the *Spectator* or the *New Statesman* might be worth while. It would not pay to advertise a special school edition of Shakespeare in the *News of the World;* but no one would be surprised to find one advertised in the *Schoolmaster.* There are different sorts of newspapers and magazines—those with a wide popular circulation like the *Daily Mail*, or *John Bull*, or *Answers;* those with a smaller circulation, mainly among people of relatively large incomes, such as the *Times*, the *Spectator*, or the *Observer*; and those with circulations, large or small, among groups of people possessing a particular interest, such as teachers, motor-car owners, farmers, engineers, amateur gardeners, photographers, Wesleyans, Trade Unionists, or any of a host of other special groups.

Anyone who sets out to advertise soon discovers that different papers charge very different rates for their space. It is sometimes said that the value of advertising space is in proportion to circulation; and to a certain extent this is true. But anyone who expects to advertise in the *Times* or the *Spectator* at the same rate per thousand of circulation as in the *Mail* or *Express* is doomed to disappointment. Man for man, or woman for woman, the readers of the

Times and the *Spectator* have more money to spend. Their individual attention is therefore worth more; and the things it is worth while to advertise in the *Times* or the *Spectator* are either relatively high-priced, such as high-class motor-cars, or wines, or cigars, or of a sort specially to appeal to the readers of these papers, such as the books which appeal chiefly to educated readers. Journals with a special appeal, again, are often able to charge rates apparently out of relation to their circulation, because all their readers may be interested in the article advertised, whereas no single advertisement is likely to appeal to more than a fraction of the readers of the *Daily Express*.

Newspaper advertising is naturally the first type that comes to one's mind; but, of course, anyone who is planning an advertising campaign has to weigh the newspaper against other forms of appeal. New books have always been advertised mainly through the press, though they are also advertised by insets in other books, by circulars from the publishers, and nowadays by posters in the Tubes. Second-hand books are advertised almost exclusively by circulation of catalogues—the only possible method, as the bookseller has usually but one copy of each book for sale. Newspapers themselves favour sky-signs, free insurances and gifts widely announced, competitions advertised in other newspapers and magazines, offers of free copies for a trial period, and of subscriptions at special rates to members of particular societies, such as school teachers. Wine merchants use both newspapers and circulated lists. Outside brokers and commission agents, for obvious reasons, use the circular as their chief instrument. The list could be multiplied indefinitely. In general, only a few conclusions can be drawn.

(1) Newspaper advertising, in journals of wide circulation, can pay only when the commodity in question is one likely to appeal to a very wide public, and is either highly elastic in demand, or subject to strong competition.

(2) Newspaper advertising, in journals of smaller but well-to-do circulation, is most likely to pay in the case of goods which are expensive, and either elastic in demand or subject to strong competition.

(3) Newspaper advertising, in journals possessing a highly specialised circulation and widely read within the group of specialists concerned, is a very valuable means of pushing commodities possessing a special appeal, especially as these are usually both elastic in demand and subject to strong competition.

(4) Newspaper advertising, in journals which are not of high standing in the category to which they belong, is seldom worth while, save at very cheap rates, or for some quite special reason.

(5) Circular advertising, of goods in wide demand, on the basis of mass circularisation, is a doubtful proposition. I am sceptical of it, save in special cases; but this is a matter of opinion, and not of knowledge.

(6) Circular advertising, in the case of specialities, is an exceedingly useful method, provided that the lists used for the purpose are really carefully selected. In the second-hand book trade, for example, the building up of a really good list of addresses is the key to success. So it is, to a substantial extent, in some kinds of publishing.

(7) Sky-signs, hoardings, and similar broadcast methods are subject to much the same conditions as newspaper advertising in journals of wide general circulation.

(8) House-to-house canvassing, where it pays, too often does so only because the canvassers are either directly sweated or compelled by circumstances to work on an insecure basis of commissions.

In all the above cases, the motive behind the advertising has been that of getting increased sales, either by increasing the total demand for the commodity, or by getting trade that would otherwise go to a rival producer, or by a com-

bination of both. When the demand is not elastic, if one firm gains, another is bound to lose. Therefore, an increase in advertising by one firm is likely to compel its rivals also to spend more in this way. When this has been done, each firm may easily have added to its costs, without gaining anything in additional sales. This is one of the commonest wastes of advertising, from both the individual and the social point of view. The remedy, not very often adopted, is a common agreement among the firms concerned to stop advertising, or at any rate to restrict its forms and the amount spent upon it.

When total demand is fairly elastic, the situation is not quite the same. For it may be worth while, from the trade standpoint, to advertise, not in order to steal a rival's trade, but in order to extend total sales. Even so, however, huge sums may be wasted if each firm pursues a separate advertising campaign of its own; for the new trade that comes from the extension of total sales cannot be distinguished from the trade that is stolen from a rival. A partial remedy in this case may be collaborative advertising. The 'Eat More Fruit' campaign and the advertising methods of the British Commercial Gas Association are instances of this tendency. Trade exhibitions, like the motor show, present a mixture of collaborative and competitive features. There is much to be said for collective advertising, wherever the main object is the extension of total sales, rather than the stealing of a rival's trade. But against it is the fact that collective advertising is apt to be impersonal, and therefore to miss something of the appeal of the advertisements of an individual firm. Even where demand is highly elastic, there is therefore a good deal to be said for an agreement to limit advertising, while keeping its personal touch, instead of an adoption of purely collective methods. This, of course, would not apply in the case of local monopolies, such as gas or electricity.

We have now reached a point at which we can attempt to sum up the gist of the argument, *from the standpoint of the individual advertiser*. The social standpoint we have still

to consider. From the purely individual standpoint, competitive advertising, designed primarily to catch someone else's trade, is a deplorably wasteful process. It may indeed pay a particular firm which manages to do it exceptionally well. But it is definitely a case of one man's gain being another's loss; and the general interest of the body of traders in the trade concerned lies in stopping it, or at least in restricting its unregulated growth. If it is left unregulated, it is terribly liable to increase, and to swell costs all round without bringing anyone any gain. If all firms in such a case advertise with equal efficiency, it is clear that every penny they spend on advertising is sheer waste. It is also sheer loss to them, unless they combine so to raise prices as to pass on the loss to the consumer. In a trade having an elastic total demand, they could not do this. When demand is very inelastic, they may be able to do so. But even so, they gain nothing, and the consumer bears a loss. Advertising in such cases is just waste.

When total demand is elastic, it is not possible to regard all advertising as wasteful from the individual standpoint. But even here unregulated advertising is exceedingly liable, under competitive conditions, to pass all reasonable bounds. It may cause costs of production to rise, despite increased demand. More often, it will not do this; but it will prevent them from falling as much as they would fall if advertising were kept under better control. There is therefore a strong case for extending, in suitable cases, the method of collective advertising, and, when this is not suitable, for the making of trade agreements wherever possible restricting the quantity and character of advertisements in the trade as a whole to that which is really needed in order to bring the additional remunerative demand into being.

Turn now to the social standpoint. It is a gain to Messrs. Cadbury if they can get some of Messrs. Rowntree's trade; but it is also Messrs. Rowntree's loss. If Messrs. Cadbury and Rowntree and other chocolate manufacturers now combine in an 'Eat More Chocolate' campaign, and the result is that they all get more trade, they all gain; and if the result is so

to lower their costs that they can sell chocolate cheaper than before, it appears as if the consumer gains too. At first sight, then, successful advertising, in the case of goods which are in elastic demand, seems to be amply justified from the social as well as the individual standpoint. But this is not the entire story. If the consuming public spends more on chocolate, will it not have less money left to spend on other things? Just as, before, Mr. Cadbury's gain was Mr. Rowntree's loss, will not all the chocolate makers be gaining at expense of the makers of other things which people now elect to go without in order to buy more chocolate?

I am not forgetting that the cost of producing chocolate may fall if more is bought. But so may the cost of producing other things rise if demand is diverted from them to chocolate. The gain is therefore not sheer gain. If the consumer now gets his chocolate cheaper, then he may have to pay more for other things because their cost of production has risen, or the makers of these other things may have to put up with less wages or less profits, or both. There is a loss to set against the gain.

Now, in one case the loss may exceed the gain, and in another the gain may exceed the loss. From the standpoint of the community, it is desirable to increase the demand for those classes of goods whose costs of production will fall most rapidly as more of them can be sold, and to decrease the demand for commodities whose costs either remain stationary or increase with growing consumption. In as far as advertising helps to achieve this result, it is on the whole beneficial, provided that it is kept within the limits necessary in order to achieve it. In as far as it does not achieve this result, or even works the other way, it is waste, from the social point of view.

Imagine for a moment a completely Collectivist State, in which all production is in the hands of the public itself. It would pay such a State to advertise wares of which it desired to increase consumption in order to decrease cost. But it would clearly not pay it to advertise for any other reason, beyond, of course, the conveying of the necessary

information about the goods and services available. Here, then, we see clearly the true social function of advertising. Its function is that of increasing consumption of those things which cost less effort to produce as demand increases, and accordingly of discouraging consumption of things to which the opposite conditions apply.

It is clear that, measured by this standard, which is the only true standard, modern advertising includes an enormously high proportion of waste. Not all, indeed, that is waste directly is waste indirectly as well. Newspaper advertising may put up the costs of the things advertised; but, of course, it puts down the price of newspapers, or enables them to grow larger, to afford better news services, and so on. A part of the sum spent on hoardings and sky-signs goes to the owners of land and buildings, who have then the money to spend. From the social standpoint, whereas the sums actually spent in printing and posting advertisements are sheer cost, because they use up capital and labour, a part of the sum spent on advertisement consists of transfers, and consumes nothing. The question in these cases is whether the transfers are socially desirable or not. Are the owners of the lands or buildings on which hoardings or sky-signs are placed more desirable recipients of the money than the people who have, as consumers of the advertised commodities, to pay the cost of the advertisement? Are our big cheap newspapers a boon worth the extra sums we have to pay for the goods whose advertisements make their production possible? But these are questions that would take me too far afield.

This paper has been a plea, not for the abolition of advertising, which is clearly impossible under existing conditions, but for a determined attempt to keep it within reasonable bounds. Just as manufacturers and traders advertise in order to sell more goods, advertising agents advertise in order to sell more advertising. They have, of course, as much right to do this as anyone else; but their calling is one which lends itself greatly to methods of 'boost', and I at any rate believe that of late years they

have been unduly successful in pushing their particular wares, far beyond the amounts necessary to take advantage of the opportunities of elastic demand, and that the result of their efforts has been an intensive campaign by each business to steal trade off the others—a campaign for which sometimes the advertisers and sometimes the consumers, but always the one or the other, are called upon to pay. I should like, therefore, to see all firms subjecting their advertising costs to the closest scrutiny; and I should lke to see—though it would hit me personally as a journalist—a great extension of agreements among firms to limit the extent and character of their advertising, with the object of cutting out that which is merely competitive and restricting the remainder to the amount positively needed in order to take advantage of the real elasticity of remunerative demand.

XIV

TOWARDS A NEW ECONOMIC THEORY[1]

CONTEMPORARY Economic Theories are all worked out upon assumptions appropriate to an individualistic type of Society. That is to say, they set out from the assumption of a 'free market' in which buyers and sellers confront one another for the exchange of goods and services, and the pricing system and the character of production are the outcome of the relations established in the 'free market'. Beginning with this elementary assumption of a 'free market', they then proceed to certain secondary assumptions—that the means of production are privately owned, that there exists a class of wage-labourers who subsist by the sale of their labour-power, that the distribution of incomes is a function of the productive system, and that these incomes are expended under the influence of free consumers' demand. Upon this basis they go on to conclude that the various factors of production are rewarded, as a part of the pricing process, in accordance with their respective marginal productivities, and that the prices of goods and services represent their marginal utilities to the consumers. Different schools of thought differ in the emphasis which they place upon the conception of the margin, in the relative importance they assign to demand factors and supply factors in the determination of prices in both the short and the long run, and in the extent to which they use the method of abstract analysis in laying down the fundamental principles of Economic Science. But, despite these differences, there is to-day a fairly wide measure of agreement among 'orthodox' economists over the fundamental economic laws or tendencies which they proclaim.

[1] A paper written for the Marshall Society, Cambridge, in January 1934.

Over against the various orthodox schools of to-day—the thoroughgoing Austrians, with their profound belief in abstract method, equilibrium analysis, and the predominant influence of consumers' demand; the more hesitant Cambridge school, linked more closely by Marshall's eclecticism with the English classical tradition, and seeking, in the contrast between the long and the short run, a compromise between the extremer adherents of supply and demand schools of doctrine; or the followers of Cassel, making the objective price-situation a third factor in the determination of economic processes side by side with the supply and demand forces—over against all these schools stand the Marxists, proclaiming a radically different gospel. But Marx, no less than the classical economists whom he criticised or their orthodox successors, set out from these same assumptions. Marx, equally with the other economists, was discussing and analysing the institutions of a Society based on private property, the 'free market', the existence of a separate labour class, the buying and selling of factors of production as well as final goods and services at market prices determined by the play of 'free' economic forces. Marx took indeed as the focal point of his analysis the relations between the *entrepreneur*, or buyer of labour-power, and the worker, with labour-power to sell. He was analysing the operation of capitalist Society, and not constructing an economic theory appropriate to a Socialist regime.

I began, however, by speaking not of Capitalism but of individualism. In the most rudimentary analysis, the assumptions underlying modern Economic Theories are individualistic rather than capitalistic. For there is, on the face of the matter, nothing capitalistic about a seller and a buyer meeting each other and agreeing upon a price, or, in the simplest case of all, on the terms of barter between their respective products. This is a relation characteristic not of Capitalism but of pre-capitalist Society. It is only at the second stage that the assumptions appropriate to Capitalism are made, when the economist fills out his

picture of the relationship between the buyer and seller of finished goods with the further detail of the buying and selling of factors of production, including labour-power. For only at this stage does the assumption of distinct economic classes make its appearance—that of a class of owners of means of production who are also buyers of labour-power, and that of a class of labourers who do not own the means of production to which their labour is applied.

In the orthodox economists, but not in Marx, the transition to these secondary assumptions is made as if it were a matter of course—merely a logical development of the original assumption of exchange in a 'free market'. The private ownership of means of production beyond what a man can operate with his own hands and its correlative, the buying and selling of labour-power, are regarded as merely extensions, involving no new principle, of the original type of exchange. Marx, on the other hand, makes this transition from simple exchange of commodities to buying and selling of labour-power the critical point in the development of the capitalist process of production. He regards the exchanging of the labour-power of human beings as involving quite different principles from the simple exchange of goods between complementary producers, and accordingly treats capitalist economic Society as resting on quite a different foundation from the primitive Societies of free exchangers of personal products.

It is of course a fundamental point with orthodox economists to deny that this difference of principle exists. Both in the simple exchange of commodities and in the more developed system of exchange which involves the buying and selling of factors of production they maintain that the same principle is at work—the exchange of equivalents. The factors of production, like final goods under both primitive and advanced conditions, tend to be sold for what they are worth, whether their various worths are conceived as measurable in values depending mainly on the amounts of labour, as broadly in Ricardo, or by their 'prices of production', as in John Stuart Mill, or in terms

of marginal utility or productivity, as by most of the modern schools. Nor does Marx dissent from this view. His theory of prices, as it is worked out in vol. iii. of *Das Kapital*, bears a close resemblance to Mill's, and he points out again and again that it is a fallacy to suppose that capitalists make their profits either by selling goods for more than they are worth or by paying labour-power less than it is worth. On the assumption that labour-power can properly be bought and sold at all as a commodity, Marx fully agrees that it tends, in the same way as other commodities, to be sold for what it is worth.[1] His difference from the orthodox economists on this point lies not in holding that labour-power as a commodity is too cheap, but in maintaining that it cannot properly be treated as a commodity at all.

Marx, then, equally with other economists, is analysing capitalist Society, and is not attempting to construct the Economics of Socialism. He would indeed clearly have regarded any attempt to construct an economic theory of Socialism as premature and Utopian; for he would have held that such a theory could be constructed only as the analysis and explanation of an already existing Socialist economy. His difference from other economists lay in this—that, whereas they regarded capitalist Society as merely developing further and elaborating the essential relations and tendencies already existing in pre-capitalist economies, he regarded Capitalism as proceeding in terms of relations and tendencies of its own, sharply marked off from the relations and tendencies of earlier economic systems.

Of course Marx, as much as any other economist, recognised that the relations and institutions of capitalist Society had developed out of earlier conditions, and were in that sense continuous with them. But he denied that this historical continuity involved identity of law or principle, and held that the process of development had

[1] I am not here concerned with the point that, owing to differing 'compositions of capital', the selling prices of commodities tend, according to Marx, to diverge from their values. For a discussion of this question see my book, *What Marx Really Meant*.

involved changes in kind and not merely in degree of elaborateness and complexity. Marx's analysis thus appears specifically as an analysis of the laws of capitalist production; whereas orthodox economists, emphasising the continuity of development from primitive to capitalist conditions, thereby present their laws as laws of economic 'nature', not confined in their operation within the limiting conditions of any one set of economic institutions.

When, however, orthodox economists assert that the laws of economics, in the form in which they set them forth, are valid absolutely, and not merely within the assumptions of Capitalism, they can mean only that they are valid within any system based on individualist institutions. For, if the assumptions of the 'free market', of the private ownership of the resources of production and of the goods emerging from the productive process, and of the exchange of these goods at prices determined by the higgling of the market are removed, the very foundations on which these laws rest are knocked away. It is possible to claim that they are valid for both 'primitive' and capitalist conditions of exchange; and it is also possible to urge that a Society based on social ownership of the means of production would be wise to preserve as much of them as it could, and to be guided largely by them in the arrangement of its economic affairs. But it is not possible to contend that to a Socialist Society they would any longer present themselves as objective laws, compelling observance and operating even in face of the will of that Society to abrogate them in favour of other principles of economic action.

For clearly the assumptions appropriate to a Socialist Society are very different not only from those appropriate to Capitalism but in certain respects even more from those appropriate to a primitive Society in which individual producers exchange the products of their personal labour. The economics of Socialism are fundamentally far more like those of Robinson Crusoe than like those of any Society in which the 'free market' is the primary economic institution.

Nor are 'Crusoe' economics in fact a whit more unreal than the picture of a Society in which the dominant system is that of the exchange of products by free individual producers. A Crusoe Society, if that is not a contradiction in terms, can exist on a desert island; but the Society of purely individual free exchangers never was on earth. Primitive institutions are not in the least like the 'free market' in which individual producers exchange goods in accordance with the efforts and sacrifices involved in their production, or the amounts of satisfaction which they are deemed capable of affording. Primitive Societies have their own economic institutions and economic laws; but these are not the laws or institutions of the simplified 'free market' of the primary equilibrium analysis. Fully as much as the economics of Robinson Crusoe, the economic theory of the pre-capitalist 'free market' is an abstraction.

It is, however, an abstraction highly suitable as a basis for the analysis of capitalist Society in a certain phase of its development—the phase in which Capitalism is highly competitive, labour unorganised, and the State disinclined to intervene in economic matters save in the police function of safeguarding the sanctity of capitalist property and protecting the essential capitalist institutions. For, at this stage of Capitalism, the laws of the 'free market' are left to work themselves out more fully than at any other point in human history. Labour is just a commodity, to be bought and sold like any other commodity in the market. Competition among *entrepreneurs* does hand over the regulation of the productive system to the possessors of spendable incomes, that is, of effective demand. The factors of production—or rather their owners—do tend to receive rewards corresponding to their marginal productivities at a commodity valuation. And the fact that private property in the hands of a limited class constitutes a monopoly, and confers monopolistic power on its possessors against those who do not share in the ownership of the means of production, is concealed by the number and internal competition of the monopolist class.

But, as we are all aware, the further progress of Capitalism makes this picture of a 'free market' Society of competing producers and consumers correspond less and less to economic realities. For with this progress there comes an immense growth of sectional monopolies, apart from the general class-monopoly of ownership; and there comes also a gradual change in the character of State activity. Particular prices, both of goods and services and of the factors of production, are more and more affected by these monopolies and by the intervention of the State; and the State further intervenes to affect the distribution of incomes by transfers accomplished through taxation. In these changed conditions, prices become less and less the simple result of market bargaining between numerous individual buyers and sellers, and more and more the result of corporate decisions originating from the side of suppliers within the limits set by the range of demand. Prices, instead of being fixed in the market, become to an increasing extent objective factors to which the market conforms. Professor Cassel's picture of prices influencing supply and demand fully as much as supply and demand influence prices comes to be a far truer presentation of the normal state of affairs than the old picture which represented price simply as the product of the contraposed forces of supply and demand.

This is not to say that the old laws of nascent Capitalism cannot be adapted to meet the changed conditions. They can be, and they are; but they lose in the process much of their old assurance. A widening range of indeterminateness in the terms of economic bargaining has to be admitted; and big differences arise among economists as to the effective amplitude of the pressure exerted on prices by trusts and combines, by Trade Unions, and by every form of sectional monopoly, as well as over the effects of States intervening to regulate prices or to redistribute incomes. The same laws can be said to be still at work; for the basis of Society remains that of private ownership, even when the effective ownership has become largely corporate instead of individual. Sectional monopolies never abrogate

competition, though they limit and regulate it. Even if the price of every class of goods were regulated by a complete sectional monopoly, even if all kinds of labour were 100 per cent organised, even if the State redistributed incomes to the greatest extent conceivable under Capitalism, competition would still go on, as long as buying and selling went on; for different products produced under the auspices of different combines would still be competitive in accordance with the consumers' power of substitution, and the different factors of production would still be competing with one another for employment. The underlying law of the market can be made to work very differently by the existence of sectional monopolies and State intervention; but as long as there are both consumers exercising choice of purchases and more than one producer is seeking to extract as much profit as possible by supplying them, the law of the market does remain in being, however differently it may work from the law of the market under the abstract conditions of simple equilibrium analysis.

But in a Socialist economy this is no longer the case. For, to the extent to which the economy is Socialist, there is only one producer, and accordingly all competition between producers has absolutely ceased, unless it is maintained artificially by dividing up the economic organisation of the Socialist Society among a number of artificial units, which are then encouraged to go on competing one with another. Of course, a Socialist Society *could* behave in this way; but, if it did, the competition which it set up would be purely artificial, and not, like capitalist competition, inherent in the economic system. It would be a competition which the Society would be free at any time to abrogate altogether, or to modify to any extent—a competition which, if it existed at all, could exist only on terms set and controlled by the Society, a 'managed' competition, to adopt a word from the field of monetary policy.

This is not at all invalidated by the fact that a Socialist Society could preserve, to any extent that it desired, the institution of free consumers' demand. The consumers

might be left free to spend their incomes exactly as they chose among the goods and services available for purchase at the prices charged for these goods and services. But every one of these factors would be of necessity a controlled factor. The goods and services available would depend on what the Socialist economy had determined to produce; the prices charged for them would depend on what it might decide to charge; and, last but not least, the incomes available for purchasing the goods and services would depend on the nature of the distribution of incomes determined upon by the Socialist economy. It is true that the Socialist governing authority might decide to interfere as little as possible with all these things. It might leave incomes to be settled by collective bargaining between the various groups of public employees and the managements of the various public 'concerns'. It might leave these concerns to adjust their production and their prices to market conditions in precisely the same ways as these adjustments are now made by capitalist combines. It might, in theory, behave as if it were not a Socialist Society at all, but only a collective economy carrying on the capitalist tradition. But to behave in any of these ways would be for it a matter of choice and policy, and not an inherent necessity of a Socialist regime; and it is in fact quite unthinkable that a Socialist Society would act in this way. For the Society would have the power actively to control all these forces; and to abstain from the active use of this power would be not to forgo it, but to employ it in a passive instead of an active way.

In essence, a Socialist economy is by the very nature of the case a planned economy. In taking the ownership of the means of production into its hands, it necessarily acquires the responsibility for controlling their use. Moreover, in socialising the non-human resources of production, it necessarily socialises the human resources as well; for labour can be used as a productive power only in conjunction with the non-human resources of production. In sequestrating to itself the incomes derived from the

ownership of property, it necessarily acquires the responsibility for the future distribution of these incomes, and therewith the power largely to determine the character of demand; for every redistribution of income is also an alteration in the composite demand schedule of the consumers. A Socialist Society is not merely a Society in which the means of production have passed into social ownership: it is a Society in which what is to be produced, at what prices the products are to be distributed, what incomes the individual citizens are to have, how much of its income the community is to save and how much to spend on current consumption, are all matters to be collectively determined in accordance with the ends which the collective wisdom of the community sets up as the guiding principles of its economic policy.

The economist, even if he has Socialist leanings, is apt at this point to shrink back appalled. For, if this is really the position, the advent of Socialism means unlearning everything he has ever learnt, or at any rate learning it afresh in a greatly altered form, and building up Economic Theory again from the very foundation. As the doctor distrusts and rejects the bone-setter, even the Socialist economist is apt to distrust and reject so devastating a conclusion, and to plead for the retention within the framework of a Socialist Society of some at least of the economic principles he has learnt. Surely, he argues, it will remain as true under Socialism as it is to-day that the free demand of consumers offers the best assurance that the maximum sum-total of satisfactions will be provided by any given supply of productive resources. Surely this involves that Socialist planning of production should proceed as a response to free consumers' demand, and not as the *fiat* of a Socialist directory. Surely, in order that the free market may continue to work, prices should still be determined by the interplay between costs of production and consumers' demand. Surely, if we abandon these sound principles of maximum utility, we shall be lost in an uncharted sea, without any compass to guide us back to land.

But—can a Socialist Society really act in this way? What will 'costs of production' be in a Socialist economic system? The costs of production consist to-day ultimately of the incomes paid out to the factors of production—of rents, interest, wages and salaries, fees, and, according to the orthodox conception of costs, normal profits. With the socialisation of the factors of production, rent, interest, and profits, or what used to be rent, interest, and profits, will presumably accrue to the Society itself, as far as they continue to exist at all. As for wages, salaries, and fees, if they continue to exist they will presumably be paid out at rates publicly determined; for we can hardly suppose that a Socialist Society will leave them to the higgling of the labour market. It will be inevitably for the Society as a whole to decide, directly or through the appropriate functional agencies, how much, if anything, to charge the various industries for the publicly owned means of production which they employ, and how much, if anything, to pay out in remuneration for work done to the human agents of production. I say 'if anything', because it is possible that a Socialist economy may decide not to distribute incomes at all in this way, but instead to distribute them all as social dividends, in accordance with the Socialist principle, 'From each according to his abilities: to each according to his needs'. Whether or no, it is plain that the costs of production, measured in terms of money —for I am assuming so far the continuance of a money economy—will be all controlled costs, determined not by forces apart from the collective mechanism of the Socialist Society, but, through that mechanism, as fundamental matters of social policy.

Perhaps it is plain now why I suggested a little while ago that 'Crusoe' economics come nearer to furnishing a basis for Socialist economy than the no less abstract economics of simple commodity exchange. For the basic problem for a Socialist economy is, like Crusoe's problem, simply that of discovering the best practicable distribution of the available productive resources; and this problem has to be

faced, as it had to be faced by Crusoe, not in terms of money costs, but directly in terms of efforts and sacrifices, the expenditure of scarce productive resources, in relation to the satisfactions to be secured from the products of economic activity.

I know it is sometimes argued that a Socialist Society should confine its 'management' of the economic forces to determining the amount of money income which each member of the community is to receive, and the amount to be expended publicly on the work of government and the provision of social services, and should then leave the consumers full freedom of choice in the expenditure of the money incomes thus socially accorded to them. If this were done, Socialist planning, it is said, would be left to adapt itself to the consumers' demand arising out of this collectively ordered distribution of incomes. But this does not answer the problem. For consumers' demand can express itself only in price-offers for goods on the market, or as a response to prices placed upon goods offered for sale. If goods already exist, the consumers can decide at what price they are prepared to take the entire supply. If prices exist, the consumers can decide how many of each class of goods they are ready to buy at these prices. But there is no such thing as a schedule of consumers' demands existing in independence of prices or of goods actually on the market. Before the consumers can decide what they are prepared to buy, someone must decide for them either what is to be produced, or at what prices goods are to be offered for sale. Under private ownership systems, this works itself out through the interplay of consumers' demand and producers' willingness to supply, acting upon an existing price and output situation. But this situation and this willingness to supply depend upon costs which are themselves fixed by the terms upon which the factors of production can be bought. In a Socialist Society, the prices of the factors of production will inevitably be determined by collective decision; for it will be necessary to decide in this way not only the level of wages and salaries but also

the price, if any, to be charged to each industry or enterprise for the use of land and of the instruments of production. It is indeed possible to conceive of Socialist enterprises determining the rent of land by bidding one against another for its use; for land is naturally limited in quantity. It is also possible to conceive of them as fixing the rate of interest by bidding one against another for shares in the available supply of capital. But the conditions of such bidding would, even so, depend on the total amount of capital available; and the supply of capital is not fixed in the same way as that of land, but must depend on the collective decision of a Socialist economy about the amount to be set aside as capital out of the national income: so that the rate of interest cannot be under Socialism a 'natural' rate, but must be a rate set by collective decision concerning the desirable ratio between capital accumulation and spending on current consumption. There can, if it is so desired, be a rate of interest under Socialism; but it is bound to be a controlled rate, determined by the collective decision of the Socialist economy.

Costs, then, will be under Socialism controlled costs, arising out of collective decisions about the use to be made of the available real resources of production. It will be possible, *after* collective decision as to the amount of saving and as to the remuneration of the human factors of production in connection with the productive process, to leave the various industries or enterprises to bid one against another for supplies of land, capital resources, and labour—this last in terms of the eligibility of the conditions offered—and to fix the prices of their goods in accordance with costs, thus relating production to consumers' demand by the interaction of supply schedules and demand schedules; but, even if this is done, both the schedules will be controlled schedules, the former being controlled by the social determination of wages and of the supply of capital, and the latter by the social determination of the distribution of incomes, both as wages and in any other form in which it may be decided to distribute them. The free

market can continue to exist only within the limits set by the social determination of the general conditions of both supply and demand.

It is, however, most unlikely that a Socialist economy will actually work quite in this way. In the first place, there is the question how far it will continue to distribute incomes as rewards for services performed in production, or how far it will substitute for wages and salaries social dividends based on the conception of need, and thus progressively divorce the payment of incomes from all direct connection with the productive system. Secondly, there is the question how far it will continue to charge rent or interest for the use of land or capital. And thirdly, there is the question how far it will continue to be guided in the planning of its economic activities by consumers' effective demand, expressed in price-offers, or how far it will adopt alternative criteria for deciding what to produce.

On the first of these points it is clear that the Socialist precept 'To each according to his needs' is entirely inconsistent with remuneration according to work done or service performed. For plainly men's productive capacities do not correspond at all to their needs. Working upon the principle of need, a Socialist Society may decide (*a*) to supply certain goods in limited quantities free of charge to all, (*b*) to supply certain goods free of charge in unlimited quantities, (*c*) to apply a certain part of its productive resources to the provision of services for collective consumption or use. To the extent to which these methods are adopted, the range of the market in which consumers make price-offers for goods or buy goods at the offered prices is narrowed; and the social product becomes a matter for collective decision and not for individual consumers' choice.[1] A certain part of the social production will accordingly be removed from the price market, and trans-

[1] This is not wholly true of goods supplied free without limit; for the consumers are left free to decide how much of each kind of goods to demand.

ferred definitely to the realm of collective decision about what is to be produced.

But the precept 'To each according to his needs' is not limited in its application to things supplied in these ways. It applies to the entire distribution of income, making any remuneration dependent on the quantity or quality of the individual's output an unsocialistic survival of individualist practices. In a transitional system, some element of remuneration according to work done will doubtless survive; but it will be as the continuance of an unsocialistic practice within an imperfectly Socialist economy. We must accordingly envisage at the least a progressive shrinkage in the labour costs of production, as incomes come to be distributed less and less as remuneration for work done, and more as social dividends according to need.

Secondly, there is the question of interest. How far will a Socialist economy continue to charge up against its various productive enterprises interest on the capital employed in them? Clearly it need not do this unless it likes; for we may assume that in a Socialist economy the accumulation of capital will be a collective function, and will take the form of a collective decision on the part of the Society as a whole to set aside a certain proportion of its current productive resources for the making of new capital goods, leaving the remainder to be applied to goods of consumption. We may assume that this decision will be made effective, not by the taxation of private incomes, but directly, and that only so much will be distributed as incomes to the citizens as will suffice to buy the current output of consumers' goods. There will accordingly be no interest payable on capital unless the community decides to pay interest to itself, by causing its sectional productive organisations to pay over to the central financial authority interest on the capital embarked in their undertakings. It is, however, most improbable that a Socialist Society will decide to finance its budget in this way. It probably will exact from each productive undertaking, except such as it decides deliberately to run at a loss, an annual

contribution to the public budget, to be used in defraying the costs of non-revenue-producing public services and of such industries as are not expected to pay their way. But it is most unlikely that this charge will be levied at a fixed rate corresponding to the amount of capital locked up in the undertaking. It will be rather in the nature of a rent than of an interest charge, and will be based rather on the ability of the industry to pay than on an estimate of the amount of capital embarked in it. Of course, the ability to pay will depend upon the prices which the industry is allowed to charge for its output; and in effect the central public authority will be assessing the prices to be charged and the rent or tax to be paid to the State as two mutually dependent magnitudes.

This, however, does not dispose of the question. For, even if interest on capital will not be actually paid, it does not follow that it will not continue to be computed, as an essential element in the real cost of production of every commodity. The accounting technique of a Socialist economy may, both in this respect and in respect of rents and wages, differ greatly from the actual payment made for the use of the various factors of production. For, as many economists have pointed out, it will be necessary, or at any rate desirable, for a Socialist Society, whatever methods it may adopt in distributing incomes or in levying taxation, to know as accurately as possible the real costs involved in the various processes of production, in order to arrive at correct judgments concerning the best distribution of the available resources of production between alternative employments. It will be necessary to have some standard for judging between the relative desirabilities of different uses of capital and labour, and between different minglings of labour and fixed capital in the execution of any particular type of work. For, in order to judge on these points, it is desirable to know not only the relative utilities of the prospective products, which may be a matter for social judgment based on the estimate of needs, but also their respective costs, in terms of the real amounts of pro-

ductive resources that will have to be used up in producing them.

On this ground, certain economists have concluded that a Socialist economy will not be able to dispense with interest, as an accounting notion, even if it no longer exists as an actual payment. In a sense this is true; but the 'interest' of Socialist accountancy will necessarily differ profoundly from interest as it exists to-day. Interest under Capitalism is a contractual payment for the use of borrowed money, fixed for varying periods and at varying rates in the case of different loans. But in Socialist 'interest' there can be no element of time-contract; for a community, like an individual, cannot enter into a contract with itself. The real 'interest' that will be of concern to a Socialist economy will be, in effect, not a sum of money at all, but the equivalent value of a quantity of real productive resources locked up for a certain period of time; and the important thing will be to know, not the rate at which interest is chargeable, but the real amount of the productive resources locked up, and the period for which the locking-up is to last.

It is, however, impossible to express qualitatively different things in commensurable terms except by expressing their measurable characteristics in a universal quantitative form. This function is performed under Capitalism by money, the 'universal equivalent', which is used as 'money of account' to make commensurable the entire range of qualitatively different things that are eligible to be bought and sold. We have learnt already to differentiate between money as a standard of value and money as a medium of exchange, and to explain that it is qualified to serve as a medium of exchange because it possesses the quality of serving as a standard of value. In a capitalist economy, where the factors of production are constantly subject to exchange, the standard of value and the medium of exchange have to be the same. But in a Socialist economy, in which the factors of production are no longer treated as exchangeable on commodity terms, the need for this

identity no longer exists. All that is required in respect of the factors of production is a standard of commensurability which will allow one factor to be weighed against another in terms of real costs.

Where, however, is such a standard to be found? It is often asserted that it cannot be found at all, and theoretical economists often dismiss Socialism as economically untenable on that ground alone. For, they tell us, the commensurability of qualitatively different things in terms of money proceeds from the fact that these things are actually weighed one against another in the market, and bought and sold for money at prices depending finally upon consumers' preferences: so that the relative values imputed to them are not arbitrary, but arise out of the actual capacity of the various things to satisfy human desires. A Socialist economy, on the other hand, will, it is asserted, have no means of economic measurement at all unless it continues to let the prices of goods be regulated by consumers' preferences, and the prices of productive agents be derived from the demand prices offered by the consumers.

To assert this is, however, to claim for the individual preferences of consumers armed with incomes arising in the course of the productive process a superior validity to that allowed to collective preferences based on conceptions of social need. This view depends on individualist assumptions: it exalts the effective demand of the individual consumer into a principle of nature, irrespective of the forces which determine the distribution of incomes—forces which, as we have seen, lie deep down in the institutional basis of Society. Consumers' demand, as it exists in any particular situation, is a reflection of the economic institutions of the Society in which it exists, and is alterable to any degree by means of an alteration of these institutions. Doubtless, given *any* distribution of incomes, there will correspond to it a schedule of effective demand on which a price structure can be based; and doubtless the actual distribution of incomes in any Society is in part the outcome of the actual state of demand, as well as a force influencing the state of

demand. But the state of demand acts upon the prices of the factors of production only within the conditions set by current social and economic institutions.

If the institutions of a Society are fundamentally individualist, there corresponds to these institutions a price-structure based on individualist assumptions, and a rewarding of the factors of production in accordance with their marginal productivities under the current conditions of private ownership. The necessary criterion of worthwhileness in such a Society is found in the preferences of individual or private consumers, as these express themselves in terms of prices. But to a Society based on collective ownership of the means of production a different criterion is appropriate; and this can be nothing else than the criterion of social need. This does not mean that a Socialist economy will pay no regard to the preferences of its individual members; but it does mean that it will consider them as valid only within limits set by its collective judgment of the needs of the community. Its primary criterion will thus be need rather than desire, and desire will be left free to secure satisfaction only to the extent of its consistency with the satisfaction of socially estimated needs.

This conception of social need is fully as objective as the conception of a market situation determined by the varying subjective desires of a number of separate consumers. It involves substituting the Society as a whole for the individuals who compose it as the authority which is to settle the use to be made of the available productive resources. But on what basis is Society, through its appropriate economic organs, to arrive at such a decision? For Society the relevant questions to ask about any economic process, in order to estimate its worthwhileness, are not only how much the goods will be desired, or needed, but also what the *real* cost of their production will be, in terms not of money but of the amounts of the 'scarce' resources of production that are to be used in producing them.

It follows from this that a Socialist economy will need to

be equipped with some means of measuring against one another the 'values' of the various factors of production, but will not need to secure the commensurability of these 'values' with the selling prices of consumers' goods. There will need to be, not a single system linking together all 'value-prices' in terms of a universal equivalent, but two distinct commensurabilities, one of products offered for sale one with another, and the other of the scarce factors of production one with another. Between these two systems of measurement there will need to exist no quantitative connection.

I have pointed out earlier in this paper that in the Marxian system the 'values' of particular commodities have no tendency to be equal to the prices at which they are sold. Value and price constitute two different systems, connected only in the sense that they both relate to the same totality of productive operations. Marx, concerned only with the critique of Capitalism, and not with the building up of an economic theory of Socialism, pushed this dualism only as far as he required it for the purposes of his critical analysis. We, at a later stage in social development and with the object-lesson before us of the actual building up of a Socialist economy, are in à position to advance a step further, and to conclude that, whereas the price system described by Marx and his orthodox rivals is the correct expression of the 'values' of a dominant capitalist economy, Marxian value is in reality the indispensable concept for a Socialist economist intent on building up a ' value' theory appropriate to the fundamental economic task of a Socialist community—the collective determination of the uses to be made of the available factors of production.

Marxian 'value' is, of course, measured by the amount of socially necessary labour incorporated in any commodity. It is simply the quantitative expression of that amount of labour. But how is one kind of labour to be measured against another? Marx's answer is made in terms of the Subsistence Theory of Wages, that is, of the quan-

tities of labour required to produce the commodities needed to remunerate the labourers of the various types required, in such a way as to induce and maintain the required supply of these types of labour. This argument has often been criticised as circular, as logically it is, in the last resort. But behind it lies a fundamental truth—that all expenditure of labour is the using up of a scarce factor of production, and that, as different kinds of labour have clearly different capacities to produce 'utilities', it is not irrelevant what kinds of labour a particular act of production uses up, and the productive capacities of the different kinds of labour must clearly be commensurable in terms of the 'values' of the utilities they can be used to produce.

But, as we have seen, the Socialist standard of utility is found no longer in the price-preferences of private consumers, but in collective estimates of social need. Accordingly, the 'values' of the various kinds of labour—which, be it remembered, have nothing to do with their prices, *i.e.* their wages; for we are assuming a quite different Socialist principle for the distribution of incomes—must depend on their varying capacities to generate utility as measured by the standard of social need. The 'value' of any sort of labour, from the standpoint of a Socialist economy, is the 'value' of the utilities which it can be employed to produce. This 'value', unlike Marx's 'value of labour-power' under Capitalism, is accordingly determined not by the amount of labour required to produce it, but by the amount of final utility which it can produce.

In other words, when the standard of utility is social, the standard for the measurement of labour value must be social too. The Socialist economy, in terms of its estimates of the scarcities of the different types of labour in relation to its estimates of social needs, will be in a position to impute 'values' to these different types of labour, and to revise its values as scarcities increase or are relieved by the provision through training of additional supplies of labour of the requisite types. A socialised service which uses up a larger amount of a scarce kind of labour will be

debited with a greater accountancy cost than a service which uses up the same amount of a less scarce kind of labour.

In this sense, and in this sense only, will labour costs be commensurable, in accordance with the cost-accountancy principles of a Socialist economy. But how, in such a case, will the 'values' of the different sorts of labour be commensurable with the 'values' of the different sorts of capital or land used up in production? Clearly this commensurability is required as a basis for judging both between the worthwhileness of alternative forms of product and between alternative methods of making the same product with different admixtures of labour, capital, and land.

It is necessary to distinguish at this point between the use of land and capital resources already in existence and the provision of new capital resources or the improvement of existing resources. For the real return upon existing resources is in the nature of a 'real rent', which can be extracted only if they are used within the limits of utilisation set by their existing condition, whereas the provision of new or improved capital resources is a process which involves the forgoing of the alternative things which the resources used in supplying them could have been employed to produce. The existing resources are already more or less narrowly specialised, whereas the new resources become specialised only when they are made. The decision to provide new or improved resources is thus a decision to apply existing resources in a particular way. It is a direction of a certain part of the labour, land, and capital resources available for social use.

The 'value' of new capital resources thus resolves itself into the 'value' of the labour and the existing resources used in making them. We can therefore resolve the entire problem of the 'value' of capital into that of the use to be made of, and the valuation to be put upon, the existing capital resources. Clearly these resources are to be valued in precisely the same way as labour, by their respective

scarcities in relation to the utilities which they can be used to produce. And, no less clearly, the valuation of existing capital resources as against labour has also to be made in this way. The question whether it is expedient, for the supply of a particular type of product, to use more or less labour in relation to land or capital, or land in relation to capital or labour, or capital in relation to labour or land, depends simply and solely on the relative scarcities of these alternative factors of production, the scarcity being estimated, as before, in terms of the social need for the types of utility which they can be used to produce.

What does this mean in practice? That there will exist in a Socialist economy a Socialist technique of cost-accounting, and that it will be the task of the Socialist cost-accountant—apart from the pricing system, though his calculations will be available for use in the subsequent process of price-formation—to attribute 'values' to all the factors of production, on principles derived from conceptions of social need which will come to him from the public planning departments concerned with the ascertainment and assessment of need. It will be his task to express these 'values' in commensurable terms for all the factors of production, but not necessarily in money terms or in terms commensurable with those used in the pricing of final products. For the factors of production will need to have only 'values' and not prices.

I am of course aware that in leaving the question at this point I am leaving a whole host of problems unsolved. Of these problems I have every intention of writing more fully elsewhere: indeed I have written, though I have not yet published, a good deal about them. My purpose in this paper has been merely to break the ground, and to bring into relief the point that the value theories appropriate to a Socialist economy differ fundamentally from those which accompany the development of Capitalism. For all theories of value are necessarily relative to the assumptions, institutions, and objects of the Societies in which they grow

up. The values which they impute are the economic expressions of the social values recognised as valid within the institutional structure of the Societies in question. The value theory of developed *bourgeois* Society is that of marginal utility, based on recognising as ultimate the dictates of consumers' demand, and not recognising that this structure of demand is the result of a distribution of incomes which itself proceeds from the institutional conditions of capitalist property. The value theory of a Socialist economy will clearly differ radically from this, because it will no longer rest on private ownership of the factors of production, and because it will employ as a *final* criterion of utility in directing the forces of production not private consumers' preferences but the collective estimation of social needs.

XV

LOYALTIES[1]

'I hate half-hearted friends. Loyalty comes before everything.'
'Ye-es; but loyalties cut up against each other sometimes, you know.'
GALSWORTHY.

A GOOD many years ago, I read to the Aristotelian Society a paper under the title 'Conflicting Social Obligations'. This paper is essentially an attempt to develop the line of thought which I then sketched out. In most of the books that I had read on Political Theory, the starting-point and the centre of the study seemed to me to be wrongly conceived. Most writers, despite their disclaimers of the abstract contrast, seemed to me too much dominated by the problem of 'the State' and 'the individual', too much concerned with the search for an ultimate principle of 'the individual's' obligation to 'the State', and too much inclined, in seeking an answer to this problem, to simplify the study of sociality in such a way as to make it valueless as a guide to the practical questions of politics and social organisation.

This artificial simplification of the problem, I felt, beset the 'metaphysicians' fully as much as the 'individualists'. The latter, indeed, presented the contrast in a cruder fashion, treating the State as an artificial mechanism devised for the furtherance of individual aims, and therefore lacking any capacity for natural or teleological growth. But the 'metaphysicians', as Professor Hobhouse has called them, were equally the victims of this error. They had seized, from Rousseau and Hegel, the vital truth that Society is natural and that its life consists in the development, in some sort, of a common or general will. But they had assigned these real attributes of sociality to a

[1] A paper read to the Aristotelian Society in March 1926.

'State' still conceived far too nearly in accordance with individualist conceptions of structure and practical function. That which belongs properly to the 'State' of Rousseau they were disposed to assign to the 'State' of Locke and Bentham. The metaphysical theory of sociality became in their hands a most dangerous and misleading metaphysic of political government.

In my first expression of my reaction from this point of view, there was a good deal of crudity. I came face to face with 'the State' as I found it, in the form of a practical political instrument; but I could find no correspondence between its working and the metaphysical theory which I had been taught. One might, of course, have become aware of this contrast—as many do—without discarding the metaphysical doctrine. But I wanted a practical guide. An ultimate principle of obligation and a teleological view of 'the State' did not help me unless I could find some relation between them and the practical problems in which I was concerned. I perceived that, in the past, theories of politics had borne a close practical relationship to political affairs. From Plato to Aquinas, from Grotius to Bentham and Rousseau, not one of the great political thinkers was a mere academician. T. H. Green himself was as much an interpreter of Victorian Liberalism as Locke was of the English Revolution. But the contemporary theorists on whom I was brought up seemed to me mere academicians both in their own thinking and in their interpretation of the great thinkers of the past. The search for the principle of political obligation had become a refuge from the attempt to answer the practical problems of social organisation.

With a keen sense of this sterility, I looked at the world of social thought. Such liveliness as I found there seemed to come from writers concerned less with Political Theory than with a number of distinct practical causes and movements. In Figgis, in Sorel, and in Thorstein Veblen, in the Marxists and in such sociologists as Gumplowicz and Ratzenhofer, I found far more lively and useful political ideas than in the contemporary philosophic writers.

There was, indeed, in these latter one vital goodness. They had learnt from Rousseau and Hegel to make the naturalness of the social will their fundamental doctrine. But they had tended to narrow the conception of this will so as to find the expression of it solely in a 'State' of whose nature they gave only a metaphysical account, and no working analysis. A doctrine which in the hands of Rousseau and Hegel had been a shearing sword of politics had become, in theirs, a merely pious sentiment.

I went back to Rousseau. And I found, in his *Political Economy*, two passages which seemed to me to illuminate the whole doctrine of his *Social Contract*. Those passages I set at the head of my previous paper.[1] The essence of it was the statement of Rousseau's doctrine of the *moi commun* or 'common will', as applying not only to 'the State', but also to every form of association and recog-

[1] 'The body politic is a moral being possessed of a will; and this general will, which tends always to the preservation and welfare of the whole and of every part, and as the source of the laws, constitutes for all the members of the State, in their relation to one another and to it, the rule of what is just or unjust.'

'Every political society is composed of other smaller societies of different kinds, each of which has its interests and its rules of conduct; but those societies which everyone perceives, because they have an external and authorised form, are not the only ones that actually exist in the State; all individuals who are united by a common interest compose as many others, either temporary or permanent, whose influence is none the less real because it is less apparent, and the proper observance of whose various relations is the true knowledge of public morals and manners. The influence of all these tacit or formal associations causes, by the influence of their will, as many different modifications of the public will. The will of these particular societies has always two relations; for the members of the association it is a general will; for the great society it is a particular will, and it is often right with regard to the first object, and wrong as to the second. An individual may be a devout priest, a brave soldier, or a zealous senator, and yet a bad citizen. A particular resolution may be advantageous to the smaller community, but pernicious to the greater. It is true that, particular societies being always subordinate to the general society in preference to others, the duty of a citizen takes precedence of that of a senator, and a man's duty of that of a citizen; but unhappily personal interest is always found in inverse ratio to duty, and increases in proportion as the association grows narrower and the engagement less sacred; which irrefragably proves that the most general will is always the most just also, and that the voice of the people is in fact the voice of God.'—ROUSSEAU, *Political Economy.*

nised common interest, whether it takes shape in any formal organisation or not.

This passage set me to the study of social obligation in a new way. I recognised that, as Dr. Bosanquet said in his pointed 'Note' to my previous paper, 'the State' in Hegel is not merely a piece of political machinery, identifiable with the government, but a totality of social relationships. But 'the State', as government, easily came to be, if not identified, at least treated as the representative of this totality, and no one will deny that both Hegel and the Hegelians were concerned to stress rather the unity or universality of 'the State' than the diversity in which this unity was found. Dr. Bosanquet contrasted Hegel with Rousseau by setting Hegel's 'State' as a totality of relationships in contrast to Rousseau's 'State' as either a machine of government or the expression of a plebiscitary vote. Herein he was right enough, if the Social Contract is to be treated as by itself the quintessential and complete outline of Rousseau's doctrine. But it was Rousseau's *Political Economy* and, incidentally, the first unfinished draft of his larger *Social Contract* scheme, that helped me to a different, and I think, a more vital, way of interpreting his thought. Of course, I do not suggest for a moment that Rousseau was either a systematic or an entirely consistent thinker. Such systematisation as he attempts in the *Social Contract* tends to spoil his idea. That idea is more vital in these earlier expressions of it.

Rousseau, then, helped me to see the same underlying basis of common will as the sustaining force, not only of 'the State', but of all associations and of all informal human groupings. And he led me to just what I wanted—a principle which would guide me in the study of the parts as well as the whole, and would set again in place the broken links in the chain of which ethical and political theory are, in separation, disconnected fragments. For when once we see that man's sociality is φύσει (that is, in becoming if not wholly in being, in intention if not thoroughly in fact), a matter of a natural will which is not

purely individual, we see at once man's relation to 'the State' as only one aspect, not different in kind from the other aspects, of his relation to his fellow-men, as it finds expression in his countless social contacts, memberships, associations, and loyalties.

Loyalties. In that word I more and more found my clue to the problem of sociality. I called my previous paper 'Conflicting Social Obligations'. To-day, I speak not of obligations but of loyalties—in terms not of the Kantian imperative, but of that common sentiment of us all which is the whole basis of our capacity to live and work together. 'What others give as duties', said Walt Whitman, 'I give as living impulses. Shall I give the heart's action as a duty?' It is in the living impulse, rather than in the obligation, that the secret of sociality—of the naturalness of human Societies—is to be found.

Graham Wallas helped me here enormously. His distrust of what he calls 'Professionalism' grew with him, in latter days, to an obsession. But, in *Human Nature in Politics*, he did make just the approach to the study of sociality that I needed. MacDougall and the so-called Social Psychologists I had found exceedingly unhelpful. The more I read them, the more they seemed merely to revive the older abstractions of 'Faculty Psychology' in new forms. Their classifications of instincts led me nowhere. But Wallas did set out, though he never quite reached his goal, to look at human behaviour, and especially social behaviour, with the eyes of a keen observer, attempting a real measurement of social phenomena as the starting-point for a practical valuation. From his conclusions I often dissented; but his method I saw was right.

I began then, from the standpoint of a practical interest, to attempt a survey of such social facts as came specially within the range of my observation. And more and more the problem stood out in my mind as a problem of loyalties, but no longer mainly of conflicting loyalties. It is true that the conflict of loyalties is apt to occupy a very large place in the discussion of the problem; but this is not because it

is the heart of the problem, but because it sticks out. In just the same way psychologists are apt to concern themselves largely with abnormal behaviour, and with the diseases of personality, because these things obtrude themselves on the observation, whereas normality normally does not. It is, however, just as dangerous in social theory as in psychology to mistake the abnormal for the normal, or to state the problem in terms of the abnormal, because the abnormal instances have received the closest study.

No Society, from a bridge club to a nation, could hold together unless a considerable proportion of its members felt a considerable degree of loyalty towards it. So much is, of course, commonplace. It does not exclude either the subjection of one body of men to another by force (of which the history of States affords abundant examples), or the survival, in a condition of suspended animation, of atrophied organisations maintained by their officials (of which a survey of the list of organisations in, say, *Whitaker's Almanac* will provide an overflowing crop). But these latter bodies, if they have lived at all, have at one time lived by the loyalty of their members, while the most oppressive States have been held together by the loyalty of their oppressing classes. Nothing is done without loyalty. Loyalty is the root of the tree of good and evil conduct.

Obviously, as Galsworthy says, these loyalties 'cut up against each other sometimes', as they did in the play from which this quotation comes. But this conflict, while it is to some extent inevitable, is not of their essence. And Rousseau, when he made his momentous discovery of the *moi commun* as the basis of all sociality, misunderstood (doubtless largely for historical reasons) the nature of the loyalties which exist in smaller or 'particular' societies, and their relationship to the greater loyalty which he called the 'General Will'. The following sentence gives the gist of his mistake. 'The will of these particular societies has always two relations; for the members of the association it is a general will; for the great society it is a particular will, and

it is often right with regard to the first object, and wrong as to the second.'

This sentence obviously embodies a truth. Each particular association, or clique, or group may have a will and interest of its own, which is unrelated to, or in conflict with, the will and interest both of other groups and of the community as a whole. It is indifferent to the whole community whether my bridge club plays 'auction' or 'contract', or whether, in my church, the service is conducted in a cassock or a frock-coat. It is not indifferent if the bridge-players privately mark the cards and then invite strangers to play, or if my church demands the right compulsorily to instruct other people's children in its own ethics and cosmogony; and on these points the common will of the bridge-players or the Church members may be a will not merely particular in relation to the larger will of the community, but positively hostile.

So far Rousseau is obviously right. But because the common will of a group may conflict with other wills, individual and social, and may fall foul of the 'General Will' of the community, it does not at all follow that this common will is to be regarded, in relation to the whole, as merely particular. That view of it really makes nonsense of the whole doctrine; for it involves treating the 'particular' associations as just what they are not, bodies artificial and unnatural, essentially unlike the greater body in which the 'General Will' is supposed to appear.

This does not square with Rousseau's essential doctrines; for elsewhere (in the first sketch of the *Social Contract*) he recognises that 'the State' itself is, in relation to the world of States, a particular association, and its will, in this relation, a particular will. It is, of course, in this regard a particular will; but it cannot be a particular will alone. For it cannot, by entering into relation with other wills, divest itself of its own essential character. And this character, Rousseau makes quite plain, is that of generality, not merely in the sense that it is a will of all, but in the far deeper sense that it is a will in individuals who are willing

universally. It is, as I insisted in my *Introduction* to Rousseau's *Social Contract*, 'above all a universal and, in the Kantian sense, a "rational" will'. But, if this is its fundamental character, it cannot put this nature off, or become merely particular, into whatever relations it may be caught up. It is at bottom the will of individuals taking a universal form.

We come back then to the individual as the source of will. But if the individual can will universally in his relation to 'the State', which in the world of States is only a 'particular association', so also can he will universally in those other groups, formal or unorganised, into which he enters as a social being. He may, it is true, will in his action inside such groups his own private interest or the interest of his friends or of the group instead of willing the interest of the whole. But so may he do any of these things when he is willing as a member of 'the State' or of any wider body. It may be, or it may not, that the danger of his willing in a 'particular' or an anti-social way is greater in the smaller than in the more inclusive groups. But this does not follow logically; it requires demonstration or disproof. And, if he may will 'particularly' or anti-socially as a member of either 'the State' or any other group or association, so may he in either case will universally or generally, striving to make his particular group or association a means in its measure to the good of the whole.

The realisation of this truth seems to me important. It connects itself directly with those doctrines which recognise groups and associations, not as *personae fictae* or mere creatures of 'the State' or the law, but as natural expressions of social personality—with Gierke and Maitland for example. And it is also fully consistent, as Dr. Bosanquet pointed out, with Hegel's doctrine of 'the State', and with any view which identifies 'the State' with a natural totality of social relationships. The doctrines, however, which concentrate on totality, fail to bring out the practical bearing of the truth. For the rational totality of the Hegelian 'State' is not being but becoming, and the vital question is how it is to become.

Social thinking has, of course, greatly changed during the eleven years since I read my previous paper. Since then, doctrines of political Pluralism have come greatly to the front. The metaphysico-legal doctrine of 'State Sovereignty' has gone markedly out of fashion. Following the march of practical affairs, social theorists have given the 'particular associations' a place in their systems. But even if one can take this new attitude as securely established, there is still a great deal of thinking to be done. In especial, the tendency has been so far to study the problem mainly on its institutional side, so as to admit in the particular association a natural capacity for growth and the assumption of fresh functions and purposes, and in 'the State' a nearer approach to a federative and pluralistic character. My own view of 'the State' as a particular association like and among others has by no means found general acceptance; the tendency has been rather to widen the structural form and constitution of the State so as to bring other associations within it. But I think my view has also gained ground; for it is clear that most plans for widening 'the State' as an instrument of government, or for giving it more a federal structure, leave outside a vast network of groupings and associations in which also the principle of natural sociality and growth must be entirely admitted.

This way of looking at the problem from the standpoint of institutions is valuable and necessary. But the time has come, I think, to look at it more closely from the standpoint of the individual himself. I insisted on this point in my previous paper, and it is to some extent stressed in Professor MacIver's *Community*. But it has not, directly at least, received nearly enough attention. I stated the point before chiefly in terms of the possible conflicts of social obligations. As soon as the plurality of loyalties or obligations is admitted, and various groups and associations are seen as the points of focus for these various loyalties, it becomes plain that the individual will or conscience, guided by the consideration of right, is the sole rational arbitrator of such conflicts. There is not an automatic or

overriding loyalty of right to 'the State' or to any group or association: there is a principle of universality in the mind of man, and in this lies the final standard of obligation.

So far, so good. But this way of stating the problem is really unsatisfactory. For it stresses the possible conflict, instead of the positive contributions which all these different loyalties can make to the common good. The best community is that which, in a positive fashion, establishes the closest harmony among its members in working towards a common good. This harmony is fully as much the harmony of associative and group life as of the individual life in a narrower sense. The making of 'the State', in Hegel's sense, is then the eliciting of the goodwill in us all, so that it penetrates every aspect of our life, and so that our private and associative actions tend, in the greatest degree, to take shape as contributions to the common good.

The idea from which we have to escape is that, because this good is a common good, and has about it a final unity and universality, it is therefore to be sought mainly along a single road. We have to get away from the error (historically natural in Rousseau and the Benthamites, but most unnatural and perverse in Professor Wallas[1]) that particular associations are primarily conspirators or that the will of the individual in 'the State' is different in kind or content, or naturally superior to his will as a member of any social group to which he may belong. We have come rather to the positive idea of the social will as finding its fullest expression where the wills of individuals find *their* fullest and most diversified expression through a rich variety of free associative life.

But this associative life and will, I have agreed, are, like the wills of the individuals who make it up, potent for evil as well as good. It is, therefore, a vital question whether 'particular' associations tend to encourage rather social or

[1] In what I say here of Professor Wallas I am thinking of *Our Social Heritage*—that is, of his latter-day views. I have the greatest admiration for his earlier work.

anti-social motives. Professor Wallas appears to tend more and more to the latter view; but is this opinion finally reconcilable with any save an anarchist conception of sociality? For why should men in their particular associations be more anti-social than they are either in their private lives on the one hand or in their relations to 'the State' on the other? As for the State, no one accepts Rousseau's statement that the General Will is automatically realised by the cancelling-out of particular wills; but, unless this statement is accepted, there is no *prima facie* or *a priori* reason for expecting men to act more socially in the affairs of the State than in any other sphere. Nor is there any reason for drawing such a distinction between their private and their associative actions, save in a sense which makes equally against 'the State' and particular associations.

There is, indeed, a very real and important sense in which all forms of organisation, since they involve some degree both of mechanisation and of abstraction, involve in some degree a distortion of the wills of the individuals who enter into them. Co-operation always involves sacrifices as well as gains. But, unless we take the anarchist view that the sacrifices necessarily outweigh the gains, the recognition of this fact has no bearing on our present problem. It applies to all organised group life, and perhaps in greatest measure of all to 'the State', as the largest and most complex kind of continuous association.

Men's motives are mixed, both in their private acts and in their 'State' acts, and in those acts which they perform as members of any group or association. Some groupings are, of course, far more important than others, and have far greater power to contribute a value or a disvalue to the common life, in proportion to the strength of the loyalty which they excite in their members. And if, in our fear of anti-social loyalties, we frown on this associative life, we dismember community, and deny to it essential means of social self-realisation. Nothing is potent for good, without being potent for evil also.

We recognise that both men and 'States' may be, on

balance, good or bad. But those of us who are not anarchists work for the self-realisation of man through some form of 'State' action, though we know the 'State' may turn out wrong as well as right. We believe that, on the whole, sociality makes for good, and tends towards unity of us one with another in pursuit of the common good. If this view holds good in relation to 'the State', it holds good also of particular associations, which have also their vital contribution to make to the common life.

What, then, are the causes which make for this interworking of private, associative, and 'State' life to the common good? The condition clearly is harmony. In order that there may be a common good to which all can know how to contribute, there must be at least the broad conception of a common plan. The association, like the individual, must have some knowledge of his 'place' if it is to set up for itself any satisfactory standard of social behaviour. In other words, the interworking of the associative life must be consciously and purposefully promoted. The doctrine of 'function', Plato's master-concept in politics, is vital for the association as well as for the individual.

The harmony has, indeed, its seat in the minds of the individuals. But it will be constantly thwarted in its expression, and anti-social motives will receive constant stimulus at the expense of social motives, if, for any reason, the institutional life of the community fails to correspond to its vital needs, or if 'the State', for any reason, is more concerned to thwart than to develop the associative life. For in this case the loyalties as well as the institutions get into conflict, and men, without losing their sense of the social totality altogether, set up in their minds steep barriers between their group loyalties and their 'State' loyalties. This both tends to a stressing of the particularism of the groups, and sets up a destructive moral conflict in the mind of the individual.

The political philosophers of nineteenth-century England, with all their sharp differences, tended from opposite extremes to this vice. The Benthamites in their hostility to

particular associations exalted not 'the State', but a mystical and immanent harmony to be realised by *laissez-faire* methods. They did their work of destruction, and produced for a brief space, in mid-Victorian England, the illusion of a lasting harmony. But they left out the power of association, and were therefore incapable of facing the new problems which took the place of the old. Their supposed 'harmony' dissolved in a welter of Imperialist and Socialist doctrines.

The Hegelians, on their side, with all their grip of the need for organising sociality, and for all their master's grip of Society as a becoming rather than a being, so whelmed the individual in the universal as to negate in practice the doctrine which they affirmed in theory. Refining the real will into the rational and universal, they lost hold of men as they are and flew away into the clouds. In their Cloud-Cuckoo-town, sociality could be fully expressed through a perfect scheme of universal State-hood in which all loyalties could find a co-ordinated meaning. But this doctrine, when it was brought down again to the actual world, tended to an exaltation of the actual 'State', and to a demand that everyone should treat it as the representative of the ideal State, and should subordinate all his purposes to it. In this form, it became an argument for tyranny, and an unreasoning justification of things as they are. While it recognised associative life as part of the State life, it tended in practice to regard all associations with suspicion, unless they were prepared to subordinate themselves utterly and unconditionally to the actual 'State'. In this way again, a destructive mutual conflict is aroused.

I am not suggesting that this was all the philosophers' fault. For philosophers, like other men, are creatures of their times. Nor am I suggesting that there is any way of setting up a perfect or automatic harmony of the personal and associative life. For circumstances change, and necessitate readjustments in social and political relations. And associations, being natural and not purely mechanistic groupings, have an inherent capacity for growth and

change. If a harmony is possible, it cannot be a static harmony. There is no such place as Utopia.

There is, however, a possibility of greater or less harmony in the working of the social principle. And the securing of greater harmony depends, not merely on the avoidance of conflicts and clashes of loyalties in men's minds or between rival groups or associations, but still more on the positive evocation of many different loyalties in the common service. For, if we suppress the grouping in which some particular loyalty finds its expression, we cannot rely on being able to transfer that loyalty to 'the State' or to some other grouping which we regard as more appropriate and beneficial. Loyalty is essentially a question of will, and the voluntary principle is therefore vital to it. Certain groups, such as 'the State' itself, must doubtless, from the nature of their functions, possess in a considerable degree a compulsory character. But a wide opportunity for purely voluntary grouping, and for the constant making and adapting of associations as new common purposes develop, is essential to the positive realisation of the common good.

Loyalty, I have just said, is a question of will. This is fundamental to my argument; but is it true? I can see some psychologists disputing it, and pointing to the large irrational element that is present in most of our group and associative loyalties. We are born into this group, and flung into that association, by force of contacts, rather than by any clear or conscious assumption of its purposes as our own. Few even of the most loyal members of most groups or associations have fully thought out their intellectual positions in regard to them, or completely rationalised the relationship. Indeed, there is a sense in which one cannot be quite so loyal with reason as without it. For the reasoner may see conflicts of loyalty which are not apparent on the surface.

All this is true enough; but it does not touch what I have been saying. For I am not assuming that loyalties are purely rational, any more than the Kantian assumes that men in fact obey only their 'real' or rational will.

Loyalties, as we find them, are a mass of instincts, prejudices, customary ideas, and assumptions caught up at second hand, selfish and unselfish purposes, ethical strivings and corporate egoisms, all mixed up together. But so, of course, is man, and all that the psychologists have told us of the irrational in man, and all the sociologists have contributed to our knowledge of the growth of man as a social animal, do not affect the fundamental issue. For they apply whatever course we shape, and they do not affect our aim of so arranging the world as to encourage men to act as rationally as possible, and in doing so to make their irrational subserve their rational purposes and pursuits.

At least, this is so, unless we throw up the sponge altogether. There is, of course, a statecraft (and still more a rhetoric) that appeals deliberately to the irrational and either dislikes or despairs of the rational in man. And there is not one among us who does not often attempt to heighten his appeal to the rational by what he regards as a legitimate attempt to get the irrational as well on his side. All rhetoric, all propaganda, and all controversial journalism, embody such appeals. Nor can anyone regard them as in themselves illegitimate; for what is right for the individual is right for the propagandist also. In our own lives, success depends largely on enlisting our irrational in the service of our rational beings; and this is what we ought to do. So must the politician, and so, in a less degree, must the philosopher.

This process becomes illegitimate only when we use the irrational to falsify or obscure the rational, instead of using it to heighten the appeal of the rational. The line is, of course, hard to draw; but so are all lines that are worth drawing. It is, however, plainly passed when, instead of trying to promote a rational harmony of loyalties in the service of the whole, a leader or a class attempts to substitute for such a harmony a single loyalty in which the irrational element is consciously made to preponderate. The commonest example of this is the beating of the war-

drum as the means of diverting men's attention from their rational wills to an unquestioning acceptance of the will of 'the State'. Napoleon I. was an adept at this, and he has had many imitators. It is, moreover, a thing that will inevitably be done in every overmastering crisis in human affairs.

It is, however, obvious that Napoleon did manage to attach to himself a great deal of loyalty, and to catch up to his own person a great many loyalties that he had really pilfered from other sources. If he made hay of the old 'States' of Europe, he also made hay of French revolutionary doctrines. I suppose it is facts of this order that make many people sceptical of doctrines which place loyalty at the heart of sociality. Loyalties, they say, are irrational; only obligations or duties have the rational element clearly in a position of dominance.

This is true, but unhelpful; for men are moved by obligations only in as far as they find expression in loyalties. And that community has the best chance of being proof against Napoleonic perversions which can develop the most free and full and harmonious associative life. The French Revolution unwittingly prepared the way for Napoleon by declaring war on particular associations within 'the State'. Affirming one overriding loyalty, it opened the way to the men who learned best how to exploit that loyalty. There is safety in numbers of loyalties, not because they must engender conflict, but because they compel comparison, choice, judgment. That community is likely to have the most rational citizens which has the fullest associative life.

And yet it may easily appear on the surface the most irrational. For it is easiest to get the best of an argument by banging all one's adversaries firmly over the head. The 'State' which forcibly suppresses, or keeps under, the expression and organisation of other loyalties, both presents, if it is successful, an extraordinary appearance of that unity which is easily mistaken for rationality, and does often actually succeed in evoking towards itself a fierce nationalistic loyalty. Napoleon's France and Bismarck's

Germany both achieved this; even Mussolini's Italy has achieved something of it. But such unity is in fact highly irrational, as readily appears in the external relations of the 'States' which rely upon it. A good 'State' ought to be a good member of the comity of nations; but such 'States' most emphatically are not.

The free burgeoning of associative life is, however, by no means an automatic method of securing the good health of the body politic. It is essential to good health; but 'the State' may suffer from other diseases. In particular, we have seen that harmony among the various expressions of the associative life is a vital need. What is this harmony? It depends, first of all, on a basis of common ideas and assumptions broad enough to sustain the citizens in their common life, and finding substance in a set of social institutions which most people regard as, in essence, fair and reasonable. If this condition is not realised (and it is not, over a large part of the world to-day) the basis for the harmonious working of the associative life is knocked away, and men group themselves into rival factions, and develop essentially conflicting loyalties, based upon their rival conceptions of social justice.

When this situation arises, Society is in peril until either one of the rival conceptions triumphs, and compels a reconstruction of the social order, or a new synthesis is reached. But to put the matter in this way is to ignore the vital character of such conflicts as I have been discussing. For divisions so vital do not develop without good practical warrant. They arise, as Marx made clear once and for all, from changes in the problem itself—that is, from changes in the material environment of man and in his command over that environment. Save under the impulsion of forces from outside, they do not arise in communities which are relatively static in their material life. But when the material basis of life changes swiftly, or when the character of social organisation is changed by conquest from without, the harmony of institutions is upset, and the conflict of loyalties and obligations develops apace.

Let us ignore the case of external conquest as immaterial to our present purpose. When the disturbing material forces arise within the community, there is always the theoretical possibility of adapting by common consent the old institutions to meet the new needs. But if the changes are far-reaching, they will almost inevitably give rise to deep rivalries and conflicts, because they will menace vested interests which are strongly entrenched, and cause the rise of new interests which see their chance in the new conditions. Vested interests and established associations tend to perpetuate themselves beyond the needs they arose to serve; new groups, with a sense that material forces are on their side, claim a right to ride rough-shod over others. Of such stuff are the great Revolutions of human history.

In such times, it is hard for men to distribute their loyalties. They have to make choice of their course and to cleave to it, backing their faith through right and wrong alike. This is not irrational of them; for the triumph of a cause is the only way to the re-establishment of a rational harmony. But it is an evil, though it is a necessary evil when once the point of disharmony which is its starting-point has been reached. At all times, men to some extent back their loyalties against their judgment on each particular case. The greater the disharmony of institutions, the more insistently they are led to do this. But their aim is the re-establishment of a harmony which will remove the need for such distortions of conduct.

Loyalties, then, can find free and rational expression only within a harmony which is twofold—a harmony of men and institutions one with another, on a basis of sufficient agreement about fundamental ideas; and a harmony of institutions with the underlying conditions of life, so that the institutions of Society are consistent with, and help forward, the best use of men's material resources in accordance with their power over nature. Until these major conditions are fairly well satisfied, it is of no use to expect men to behave in accordance with the general will; for there is no general will which can find expression in their associa-

tive life. Loyalties therefore tend, in such circumstances, to present themselves in the superficial form, not of contributions to the common good, but of conspiracies against the 'public'. But this is because there is no 'public' whose interests the associative life can find satisfaction in serving.

The mistake, in such times, is to denounce the particular loyalties on account of the perversions to which they are subject, and to urge their submergence in a unifying loyalty to the whole. Such an insistence is usually ineffective; for loyalties cannot be easily transferred. But it is also disastrous if it succeeds. For the loyalty which is concentrated on the general by the suppression of the particular is an irrational loyalty, liable to achieve expression in disastrous forms, fatal alike to liberty at home and to fellowship abroad. Rational loyalty to the whole is what we want; but that is to be achieved only through a harmony of diversified loyalties to the parts. The freedom of voluntary association is the life-breath of its being.

THE END

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